



University of Trento  
School of International Studies

---

# INTEGRATION IN TIMES OF CRISIS

---

*Testing Neofunctional hypotheses: a political economy investigation of crisis-led integration.*

Author: Francesco Nicoli  
Supervisor: Prof. Luigi Bonatti

Thesis submitted in partial fulfillment of the requirements for the degree of Doctor in Philosophy  
in International Studies.  
Trento, 30 September 2016

Integration in times of crisis. Testing Neofunctional hypotheses: a political economy investigation of crisis-led integration

Francesco Nicoli, Università di Trento

[Francesco.nicoli@unitn.it](mailto:Francesco.nicoli@unitn.it)

# Acknowledgments

During these three years of research I greatly benefited from the advice and support of many people. First, I am grateful to the faculty and staff of the School of International Studies in Trento, who have contributed to make this experience smoother and more enriching than I expected beforehand. In particular, I am in debt with professor Luigi Bonatti for his masterful guidance and his dedication. Furthermore, I wish to thank professors Andrea Fracasasso and Christopher Gilbert for their invaluable support in navigating the perilous waters of Econometrics; professor Simona Piattoni for her advice on integration theory, and professor Mark Beittel for sharing his experienced understanding of the subtleties of academic life and of the English language.

I also wish to thank Cinzia Alcidi, head of the Economic Policy Department at CEPS in Brussels and professor Mark Hallerberg, at the Hertie School of Governance in Berlin, for their warm welcome in their respective institutions and their valuable advice on the ways forward. In addition, I would like to thank professor Ben Crum, from the Vrije Universiteit Van Amsterdam, for his suggestions on Chapter 2.

In each of these three institutions I found supportive colleagues and good friends, who have helped me in refining the ideas and results presented here. In particular, I would like to thank Martin Duchac and Leila Giannetto from the School of International Studies; Brian Fabo and Caroline Lenearts from CEPS; and Maurits Meijers from the Hertie School of Governance. Similarly, I would like to thank my colleagues at the INET Working Group on Europe's Political Economy, who have contributed to strengthen my research with their suggestions.

Finally, I am especially grateful to Doris, who has relentlessly supported me in these years in many ways. Without her dedication in reading, revising, and criticizing my work, this dissertation would have been a very different (and substantially poorer) piece of research.



# Contents

Introduction .....	1
Part One: A Neofunctional analysis of the Eurocrisis .....	13
Chapter One: Neofunctionalism Revisited: Theories, Questions, Methodologies .....	15
Chapter Two: Crises and institutional change the long-run: an historical overview of Europe's 70 years of unintended integration. ....	41
Chapter Three: Is the Eurocrisis a Functional Crisis? A quantitative investigation of the Eurocrisis' endogeneity. ....	66
Chapter Four: Spill-arounds, but mainly spillovers? A qualitative assessment of the crisis' functional outcomes.....	107
Part Two: Postfunctionalism and the Eurocrisis .....	136
Chapter Five: Postfunctionalism and the issue of democratic legitimacy in the era of Fiscal integration.....	138
Chapter Six: Powers, Governance, Eurobonds. Did the crisis affect preferences for integration? .....	168
Chapter Seven: Hard-line Euroscepticism and the political fallout of the Eurocrisis: evidence from a 108 elections panel study .....	193
Conclusions .....	219
Bibliography .....	228



# Introduction

*“ L’Europe se fera dans les crises et elle sera la somme des solutions apportées à ces crises ”*

Jean Monnet, *Memoirs*, 1978

*“I am sure the euro will oblige us to introduce a new set of economic policy instruments. It is politically impossible to propose that now. But some day there will be a crisis and new instruments will be created.”*

Romano Prodi, *Financial Times*, 2001

## **1. Born from the ashes? Why revisiting Neofunctionalism (again) in times of crisis**

Endless articles, books and papers have begun, in the last half-century, with one of the two previous quotes. Yet, the turn of the year 2017 may sign the ninth consecutive year of crisis for the EMU, which has only inched towards a comprehensive and stable solution of its disease. While large parts of the world economy have suffered as much as Europe during the years of the global recession which have followed the collapse of Lehman Brothers in 2008, the European Union, and the Euro Area in particular, which has plunged into an even deeper crisis.

Despite the several concessions in terms of sovereignty accepted by EMU member states, an uncontroversial leap into the realm of fiscal integration –which according to many, is essential to permanently solve the EMU disease— is yet to be made. On the one hand, the Eurocrisis has generated spillovers in areas such as macroeconomic, macroprudential, banking and fiscal policy, which, “unthinkable” just fifteen years ago, are now hardly reversible. It appears that the engine of European integration – its functional integration dynamics— is once more at work. Intrinsic tensions have emerged: a majority of member-states are hesitant in undertaking the fundamental steps towards integration of “core state powers”, some of which, particularly in the field of fiscal policy, constitute a high priority for a permanent resolution of the Eurocrisis. Here lays a fundamental conundrum: Europe is affected by a self-fuelling, circular disease, as briefly suggested by Wijsman (2016). Not having yet completed its democratic structures, to achieve legitimacy it still relies primarily on output legitimacy. Precisely because democratic structures are underdeveloped, many believe that the actions required to address the crisis permanently—such as creating a fiscal union – cannot be implemented. However, without such steps, the crisis persists, thus harming output legitimacy; and as output legitimacy fades, the support for further integration weakens even more, fuelling the EMU’s Circular Illness. In other words, without appropriate powers to address the crisis, the Union’s institutions lack means to provide either stabilization or economic stimulus at central level, fuelling, in ever-growing shares of the population, a growing scepticism towards the capabilities and the usefulness of the Union. In turn, this lack of effectiveness undermines the people’s trust in the Union and their willingness to proceed with further European Integration, at the moment, probably, where integration is most needed. The Eurosceptic contagion, which began at the periphery of the Union with the electoral triumph of Syriza in Greece and dramatic vote to leave the EU in the United Kingdom, may reach core states like Austria, France and Germany soon enough.

The Eurocrisis, and the associated austerity, have generated a massive amount of academic thinking on European monetary integration and its limits, both in Political Science and Economics. For many, including Nobel Laureate Joseph Stiglitz (2016) the Eurocrisis has constituted the occasion to ramp up criticism of the international economic order: the Single Currency -which seemingly protected its members at the outbreak of the storm in 2008- has often been pictured like the true responsible of the endless crisis. Criticism of the Eurozone’s setup is enshrined in three arguments (only partially overlapping), which recur



in the recent debate. First, some claim that the very introduction of a Single Currency, eliminating the possibility for monetarization of the national debt and the manipulation of the exchange rate, is to be considered the true responsible of the European illness. Second, some consider that, although the Single Currency as such helped both in strengthening national economies and in protecting them against the 2008 financial storm, to be sustainable in the long term requires institutions and incentives able to shape the actions of national policy makers. However, such institutions and incentives failed to prompt national change and adaptation to the new conditions; national policy-makers largely continued to do business-as-usual, albeit in a different scenario. Thus, the Single Currency (and its institutions) is partially responsible for the crisis, having failed to promote national adaptation. Third, some believe that the Single Currency, as such, has no direct responsibilities: the continuing European crisis is rather due to the over-imposed austerity policies, wrongly considered as the only option to protect monetary integration. They claim a different solution existed: by letting the budget deficit increase, domestic growth could be fostered thus restoring confidence and investment (an exhaustive literature review on the Eurocrisis is provided in the first part of Chapter 3).

Despite the uncertainty surrounding the exact role of the Monetary Union in contributing to the current crisis, integration in the Euro Area has proceeded as a response to the crisis. Yet, the end of the Eurozone's troubles is still far, and further integration will be achieved in the incoming years as agreed in the Five Presidents' Report, released in Spring 2015. However, the institutions and procedures created so far, and – as far as official proposals are concerned, institutions likely to be created in the next years - present elements of fiscal and economic integration which might undermine the democratic legitimacy of the European Union. Indeed, the rise of Eurosceptic forces observed in occasion of the European elections of 2014 witnesses not only the rejection of austerity policies (which would be coherent with the traditional understanding of EU's output legitimacy) but indeed a true “integration fatigue” and a sentiment of rejection against institutions and symbols of European integration.

Yet, the wakes of a catalyzing event such as the Eurocrisis are hardly limited to the Economics disciplines. Of all those spillovers, this doctoral dissertation focuses in particular on political integration theory. In fact, of all branches of political science, scholars of international integration should have been the better-

prepared to deal with the Eurocrisis; the once-leading theory of European Integration, Neofunctionalism, enshrined within its crisis-feedback dynamics the very engine of supranational integration. But the golden age of Neofunctionalism had long passed, and its heritage notwithstanding, the Eurocrisis caught many scholars of European integration off-guard. To some extent, that “integration advances through crises” was one of the classical, old-age *adages* that everybody knows but most prefer to ignore; - despite the fact that, since its inception, crises and integration have advanced hand-in-hand (for an historical perspective on the crisis-integration dynamics, see Chapter 2).

In fact, the idea that integration proceeds through crises is all but new: it belongs to the functionalist integration paradigm. Functionalism constitutes a loose body of theories of supranational integration which original formulation dates back to the first works of David Mitrany in 1919. It has undergone several cycles of elaboration, from the original Functionalism of Mitrany (early functionalism, as defined in this work), to the Neofunctionalism (or micro-Functionalism, as it is named throughout this volume ) of Haas (1959, 1964) which focuses on agents’ interests and has been largely inspired by the behavioral revolution in social sciences; to the neo-Neofunctionalism (or macro-Functionalism as we name it here) of Schmitter (2002), based on the idea of cycles of crisis-induced integration; to conclude with the Postfunctionalism approach of Hooghe and Marks (2009), postulating “the end of the market-honeymoon” (Hartmann & De Witte, 2014) and the entry of the masses on the scene of European policy making. Moreover, functionalist-inspired arguments are present in several other disciplines, which truthfully claim at least in part an ascendance in the genesis of the theory. From Balassa (1960) and Mundell’s (1960, 1961) economic and monetary integration for economic sciences, to “integration through law” in European law studies, to Erhard and Müller-Armack’s (1978) *Soziale Marktwirtschaft* and Böhm- Eucken’s Ordoliberalism, Functionalist reasoning encompasses a vast range of social disciplines and has gathered, over time, many fundamental inputs from leading authors.

Nevertheless, as a comprehensive theory of integration, Neofunctionalism was somehow neglected and considered outdated when the crisis struck Europe. As a theory, it was deemed flawed by several well-known problems: first, it suffered from a perceived inability to explain delays, stagnation, or even disintegration: in the opinion of many scholars, the most-known (but not the most updated) version of

functionalism, dating back to Haas' 1959 seminal book was unable to explain such failures. Moreover, over time the several versions of Functionalism and its related theories have probably overgrown, loosening their connections with the original argument and with each other, to the point Functionalism, as such, lacks today the backing of the new generation of leading scholars in European integration, albeit prominent academic work has flourished in its sister and offspring fields. Moreover, perhaps as a consequence of its own overgrowth, Functionalist scholarship had suffered from the increasing influence of the liberal-intergovernmentalist school, eminently represented by Andrew Moravcsik (1998)'s work. Good timing contributed to Moravcsik's success: his theoretical claims had found, in fact, sudden empirical evidence in the intergovernmental shift of the very functioning of European Institutions occurred since the failure of the European Constitutional Treaty in 2005 by the hands of the French and Dutch voters; the clear intergovernmental management of the crisis (but not its outcomes, as discussed in Chapter 4) have somehow contributed to strengthen the liberal-intergovernmentalism's position as a leading theory of integration.

Yet liberal-intergovernmentalism, while successful as a theory of *international organization* by correctly explaining how nation states' choices reflect the domestic understanding of national economic and political priorities, fails as a theory of *integration* because it takes such interests and preferences as strictly exogenous phenomena. The added value of Functionalism, in all its incarnations, has always been to explain the endogenous dynamics that lead states to integrate over time, emphasizing the structural, path-dependency consequences that each step of integration produces. Paradoxically, being Functionalism a theory of crisis-led integration, only a handful of scholars openly referred themselves as Neofunctionalists at the outbreak of the crisis; the discipline of European Studies was lacking a solid backbone of scholarship on crisis-led integration, precisely in the moment when crisis-led integration was about to unleash.

In the wake of the Eurocrisis, the European integration debate has been marked by several attempts to move beyond the liberal-intergovernmental paradigm, with important contributions, for instance, from Kalypso Nicolaidis (2012) and Sergio Fabbrini (2016). Others have attempted to revert towards, or reinvigorate, a systemic functionalist approach to explain crisis-led integration, for instance Genschel and Jachtenfuchs (2016), Isiksel (2016), Schmitter and Lefkofridi (2015a, 2015b) or Schimmerfellig (2014). Despite the value of recent contributions, however, the principles of functional integration theory are in need of a

comprehensive revision enabling a coherent understanding of the paradigm and ensuring that its explanatory potential is kept up to date with the developments in the real world. This doctoral dissertation, rather than a self-contained exercise, was conceived and planned from its inception as a path-opening work aimed to further such a goal in a series of papers on Systemic Functionalism, both theoretical and empirical in nature. Indeed, the dissertation is structured to lay down the fundamental bricks of the common foundations upon which all functionalist approaches—micro, agent-based Neofunctionalism à la Haas, Schmitter's neo-Neofunctionalism, and Hooghe-Marks' Postfunctionalism—can be re-organized and understood in their relations.

The Eurocrisis constitutes, in my vision, the perfect occasion to strengthen and test a macro-functionalist theory of integration. A broad, two-tier research problem emerges: is the Eurocrisis a Functional Crisis, as defined by Philippe Schmitter? To what extent is the Eurocrisis politicizing the process of European Integration, as hinted by Hooghe and Marks, thereby confirming the integration hypothesis of Schmitter? The implications of this problem are far wider than the settlement of a theoretical debate; if, generally, Neofunctionalism is correct, and if the hypothesis concerning the inception of the transformation cycle is correct, it would imply that the Union has reached a point of no-return, where it either moves towards full federalization, or it risks a permanent break-up. Moreover, despite their general and theoretical formulation, the specific answers to these questions, as laid down within the different papers of this dissertation, may enrich quite different bodies of literature. Chapter 2 provides an innovative account of European Integration's economic history; Chapter 3 inserts itself in the economics' debate on the origins of the Eurocrisis; Chapter 4 contributes to the debate on crisis-led politicization of the EU; Chapter 5 provides a theoretical contribution on the fundamental challenges of the EU; Chapter 6 inserts itself in the literature on how the crisis has affected preferences for integration; finally, Chapter 7 provides an innovative approach for assessing the political fallout of the crisis by looking at electoral hard-line Euroscepticism.

## **2. About this volume**

This dissertation attempts to operationalize the quest for an answer to this broad research problem through six standalone papers clustered in two parts, plus introduction and conclusion. In addition, Chapter 1 reconstructs the key elements of systemic functionalism, guiding the reader through the theoretical pillars

of this work presenting its overall logic – questions, methodologies, and chapter connections. Part One of the dissertation (Chapters 1-4) deals with the fundamental question concerning the Neofunctional nature of the Eurocrisis, attempting to clarify to what extent the Eurocrisis can be really qualified as a “functional crisis”. Chapter 2 provides a comprehensive historical account of functional crises through the first 60 years of European Integration; Chapter 3 provides an econometric test of the endogenous nature of the Eurocrisis; Chapter 4 provides a qualitative assessment of the functional nature of the institutions introduced during the crisis.

Part Two of the dissertation (Chapters 5-7) dives into the possible Postfunctional implications of the Eurocrisis, analyzing to what extent the crisis is contributing to create a mobilized European public sphere. In particular, Chapter 5 provides a theoretical analysis of how the crisis is changing the legitimacy of the EU; Chapter 6 provides an econometric assessment of the crisis’ impact on citizens’ preferences for further integration; finally, Chapter 7 provides an analysis of the crisis’ impact on the performance of extreme Eurosceptic parties.

*A word of caution:* this dissertation is in many ways a hybrid creature. It touches upon multiple disciplines: Integration theory in Chapter 1; economics mainly in Chapters 2 and 3; European Studies in Chapters 4-7; legal philosophy in Chapter 5. I understand the risks of speaking to multiple audiences: readers from different disciplines may stumble across parts of the dissertation that she or he may consider repetitive, or excessively simplified, or simply not stimulating enough to be worth a careful analysis. However, I maintain the belief that integration encompasses different fields and requires a genuine, multidisciplinary understanding; this is therefore a risk I am willing to take.

Moreover, it is something short of a coherent book (although parts of it may one day become one) and something more than a few connected papers. Several chapters of this volume have been published as standalone pieces either in book chapters (for example Chapter 5, in an edited volume of the University of Freiburg) or in leading journals (like Chapter 7, in the *Journal of Common Market Studies*); others are currently under review (Chapters 2 and 4). In fact, the chapters of this volume, although linked together by a linear research design, have been written mostly to be stand-alone pieces of research. This may have two implications: first, precisely because they are all connected through their overarching aim and their joint

contribution to a wider research question but simultaneously they also exist as stand-alone pieces, they tend to include a section on literature review which in some cases may be overlapping. Second, the volume, overall, recurs to a wide range of methodologies which are specific to individual papers. Chapters 2 and 5 are mainly theoretical; Chapters 3, 6 and 7 provide econometric analysis; Chapter 4 applies qualitative empirical research. The rationale and the specific research question behind each of the chapters is discussed in the second part of Chapter 1, which provides a summary of Neo-Neofunctionalism and discusses models, questions and methodologies. Table A below shows the list of chapters and their current publication status.

Table A: Dissertation Structure				
	Chapter	Title	Publication status	Methodology & approach
	1	<i>Neofunctionalism revisited</i>	Not for publication. Parts of it in review along with parts of Chapter 5 (see below)	Theoretical reconstruction
<b>Part 1</b>  <i>the Neofunctional nature of the Eurocrisis</i>	2	<i>Integration through crises: a systematic view of Europe's 70 years of unintended integration</i>	In review at <i>Review of International Political Economy</i> (2 <sup>nd</sup> review)	Historical/qualitative
	3	<i>Is the Eurocrisis a Functional crisis? A quantitative assessment</i>	Reserved for INET Special Issue on Europe's Convergence and Divergence on the <i>Journal of Economic Policy</i>	Econometrics
	4	<i>Spillarounds, but mainly spillovers? Re-assessing crisis-led functional integration</i>	In review at <i>Comparative European Politics</i> (1 <sup>st</sup> review)	Qualitative/text & legal analysis
<b>Part 2</b>  <i>the post-functional consequences of the Eurocrisis</i>	5	<i>Democratic governance in times of fiscal integration: from functional to Postfunctional legitimacy?</i>	Early (2014) version published as chapter in: Krieger, T., Panke, D. and B. Neumaker (eds) (2015) <i>Europe's Crisis: the conflict-theoretical perspective</i> . Nomos Publishing.  New (2015) version in published on the <i>Journal of European Integration</i> (forthcoming)  A mixed Chapter1/Chapter 5 version in review at <i>Polish Journal of Political Science</i>	Qualitative/ political philosophy
	6	<i>Did the Eurocrisis affect preferences for integration?</i>	In review at the <i>Journal of Common Market Studies</i>	Econometrics
	7	<i>Hard-line Euroscepticism and the Eurocrisis: evidence from 108 elections panel study</i>	Published in <i>Journal of Common Market Studies</i> (forthcoming)	Econometrics

### Additional remarks

Overall, this dissertation is the result of more than three full years of research, conducted in three different institutions in three countries (University of Trento in Italy, the Centre for European Policy Studies in Brussels, Belgium and the Hertie School of Governance in Berlin, Germany). As a result, the research work carried out in these years has produced not only the papers here presented as dissertation chapters, but also several other pieces of research which have not been directly included in the dissertation due to space constraints and the need of maintaining a clearer “red wire” between the chapters. Table B provides a list of published and under-review papers written as complementary work to the main body of the dissertation.

Table B- spin-off research (published or under review)
<ul style="list-style-type: none"> <li>• Nicoli, F. (2016) Governance in the 2025 run-up: a Joint Budgetary Procedure. <i>Perspectives on Federalism</i>, Issue 8, No. 2, pp. 100-124</li> <li>• Nicoli, F. (2016) From governance to government? Towards a Genuine Economic and Monetary Union <i>Journal of Economic Policy</i>, vol. 32, Issue 3, pp. 413-440. <i>The paper won the first prize of the Italian Parliament-Eunews research competition on “how to govern Europe”</i></li> <li>• Nicoli, F. (2015) Eurocrisis and the Myths of European Redistribution: Illegitimate, Unsustainable, Inefficient? <i>Perspectives on Federalism</i>, Vol. 7, Issue 3, pp. 19-48;</li> <li>• Nicoli, F. (2014) Populism, Polarization, Politicization, Participation. Projecting the EU Beyond the Market? Chapter in <i>“Growing Populism and European Elections.”</i> Institute of European Democrats, 2014.</li> <li>• Alcidi, C., Barslund, M., Busse, M. and F. Nicoli (2016) Labour Mobility and the European Unemployment Benefit Scheme. In review as <i>European Commission Working Paper</i>;</li> </ul>

Moreover, as a part of a broader effort towards research dissemination, the papers of this dissertation have been presented in a series of international conferences; the list is presented in table C below.

Table C- summary of dissemination efforts
<ul style="list-style-type: none"> <li>• “From Governance to Government: how to organize a smooth transition”. Prize lecture given at the International Conference “How to govern Europe”, Camera dei Deputati, Rome, 22-23 November 2016</li> <li>• “Powers, Eurobonds, Governance”. Presentation for the International Conference “Piercing Together a Paradigm”, Central European University, 19-22 October 2016</li> <li>• <i>A theory of Functional Legitimacy</i>. Presentation for the International Conference “EU legitimacy in times of crisis”, Warsaw, 20<sup>th</sup>-21<sup>th</sup> June 2016.</li> <li>• <i>Is the Eurocrisis a functional crisis? Quantitative and qualitative evidence</i>, and <i>Extreme Euroscepticism and the crisis: quantitative evidence</i>, two presentations for the SGEU Pan-European Conference “The Union Constitutional and Institutional Adaptation”, June 16<sup>th</sup>-18<sup>th</sup>, 2016</li> <li>• <i>Did the Euro contribute to the Eurocrisis? Quantitative evidence from a 700 observations panel study</i>. Presentation for the Second Meeting of the INET Standing Group on Europe’s Political Economy, University of Trento, 2<sup>nd</sup>-5<sup>th</sup> of June, 2016</li> <li>• Organization and Coordination of the inception meeting of the INET Standing Group on Europe’s Political Economy, jointly organised by INET and CEPS Brussels, February 25<sup>th</sup>- 28<sup>th</sup>, 2016</li> <li>• <i>From Governance to Government? A proposal for a Joint Budgetary Procedure to overhaul the new economic governance</i>. Presentation for the International Conference “What Budget, resources fiscal and borrowing powers for the EU?” Florence, 10<sup>th</sup>-13<sup>th</sup> November 2015</li> <li>• <i>Electoral Euroscepticism and the Economic Crisis: Evidence from 108-Elections Panel Study Across Europe</i>. Presentation for the Quinquennial International Conference of the European Electoral Survey, University of Mannheim, November 6<sup>th</sup>-8<sup>th</sup>, 2015</li> <li>• <i>Solidarity in times of crisis: inefficient, illegitimate, unsustainable?</i> Presentation for the International Conference “Solidarity in Hard Times”, University of Madrid CEU San Pablo, June 9<sup>th</sup>-12<sup>th</sup>, 2015</li> </ul>



- *Democratic legitimacy in the Era of fiscal integration, and Electoral Euroscepticism and the Economic Crisis: Evidence from 100-Elections Panel Study Across Europe*. Two presentations for the Fifth Euro-Academia international conference, Barcelona, 27-28<sup>th</sup> March, 2015
- *Democratic Legitimacy, Fiscal Integration and the Governance Trilemma*. Presentation for the international conference “Europe's Crisis: The Conflict-Theoretic Perspective”, University of Freiburg, 25-26 September 2014
- *Populism, Polarization, Politicization, Participation: projecting the EU beyond the Market?* Presentation for “European Union and Rising Populism: a Challenge for Democracy” conference, Institute of European Democrats, Bratislava, 24-25 April 2014
- *The issue of democratic legitimacy in the Era of Fiscal integration*. School of International Studies, University of Trento, 8 April 2014
- *Functional and economic analysis of the building European Fiscal Union* Presentation for “Questioning Re:Generating Europe” Conference, German Journal of European Law. School of International Studies, University of Trento, 16 December 2013



## **Part One: Neofunctional analysis of the Eurocrisis**



# Chapter One: Neofunctionalism Revisited: Theories, Questions, Methodologies

## 1. Introduction

Neofunctionalism is, likely, the most known, praised and criticized theory of supranational integration. This doctoral dissertation aims to test some of its hypotheses in the framework of the Eurocrisis; indeed, it constitutes the “red wire” linking together the individual papers of this doctoral dissertation, papers that would, otherwise, be stand-alone pieces of research. Despite their stand-alone nature, the research presented in Chapters 2-7 conjures towards the common goal of modelling, testing and improving Neofunctionalism; or rather, that particular version of Neofunctionalism resulting from the intertwining of Philippe Schmitter’s Neo-Neofunctionalism, Hooghe-Marks Postfunctionalism, and several other contributions. In this framework, the goal of this Chapter is to provide a summary of the evolution and theoretical foundations of “Systemic Functionalism”, and –naturally— discuss its operationalization through a series of research questions the individual papers deal with. Before proceeding with a detailed discussion of the dissertation’s questions and research design, it is useful to briefly recall the evolution of the theoretical body of functionalism (along with the definitions of key concepts recurrent throughout the dissertation, discussed in section 3).

## 2. Hundred years and counting: Functionalism over time

Functional integration theory has a long history and has gone through several stages of revision and change. Roughly, four phases can be identified: Mitrany’s early Functionalism; Haas’ Neofunctionalism;

Schmitter's Neo-Neo Functionalism; and Hooghe-Marks' Postfunctionalism. This section provides a short summary of each stage.

### 2.1. Mitrany's early Functionalism.

Functionalism is no young theory: in fact, it's about to celebrate its hundredth anniversary. It was conceived in the wakes of the collapse of the Central Empires, at the end of the First World War. Interestingly enough, it was born not as a theory of supranational integration, but as a theory of orderly empire dismantlement by the hands of David Mitrany (1888-1975), a British-Romanian political scientist of liberal sensibility. The very early writings of Mitrany on international institutions, dating back to the period 1917-1919 and written for the League of Nations, concern the problem of peaceful competences' devolution across the collapsing Austrian-Hungarian Empire. Differently from following versions of the theory, Mitrany's original Functionalism lacks truly foundational *Oeuvre*: rather, the author introduced new concepts and continuously developed older intuitions over his entire life-time.<sup>1</sup> The evolution of Mitrany's thinking is tracked through four key publications: Mitrany (1933), Mitrany (1941), Mitrany (1965) and Mitrany (1975). Rather than a *theory of integration*, as later Neofunctionalism and its offspring would become, Mitrany's Functionalism is a normative theory of political organization.<sup>2</sup>

Mitrany's key idea, today perhaps widely accepted but rather revolutionary for his time, is quite simple: international organisations shall not be based on political sovereignty of supranational institutions, but rather are to be based on the transfer of limited competences (functions) to ad hoc institutions. In general, Mitrany's core assumption is that national constitutions aim to restrict the expansion of social and economic forces which, by nature, tend to be borderless (Mitrany, 1933, in Mitrany, 1975: 97)<sup>3</sup>; the international

---

<sup>1</sup> Mitrany (1975) provides a late organisation of Mitrany's key writings carried out by Mitrany himself in the volume "The Functional Theory of Politics", which contains a collection of relevant papers on Functionalism and interesting autobiographical references.

<sup>2</sup> The author's own words provide an excellent definition of its mature thinking:

*"The trend (...) is to organise a government following specific ends and needs, and according to the conditions in their time and place, in lieu of the traditional organisation on the basis of a set of constitutional division of jurisdiction and rights and powers"* (Mitrany, 1941: 113); *"the function, one might say, determines the political instrument suitable for [the international organization's] proper activity, and by the same means provides for its reform at every stage"* (Mitrany, 1941: 118).

<sup>3</sup> The 1975 text cites an earlier work from 1933 (*"the progress in international government"*): *"but social life, in the widest sense of the term, now rests on an intricate network of goods and services. To insist on a sovereign right to interfere with them is to assume a practical right to disrupt them."*

expansion of social and economic integration necessarily outpaces political integration. Therefore, no traditional constitutional arrangement inferior than a global one would solve the problem of the inconsistency among the development pace of social and economic interdependence and the pace of political integration. Three key organizational principles ensue: (i) *functional flexibility*: short of a global political arrangement, only functional institutions are flexible enough to adapt rapidly to social and economic integration (Mitrany, 1965); (ii) *non-politicization*: institutions should avoid redistributive policies and be mainly regulative in nature (Mitrany, 1941:114; 1975: 26-27); (iii) *globalism*: to prevent substituting national competition with continental competition, regional arrangements should be rejected in favour of global solutions (Mitrany, 1963; 1965; 1975:261).

Despite the normative nature of his contribution, Mitrany appears aware of the theoretical implications that his approach bears. In fact, despite the rejection of international federalism as a viable initial solution, he noted that – while analysing the unexpected growth of powers of the American fiscal authorities during the New Deal – “*every function was left to generate others gradually: and in every case the appropriate authority was left to develop its functions and powers out of actual performance*” (Mitrany, 1942, in Mitrany 1975:27). This rough, initial definition of *spillover effect* would then be cornerstone of later incarnations of the theory, starting from Haas’ Neofunctionalism.

## 2.2 Haas’ Neofunctionalism

Neofunctionalism is a broad theory, encompassing many subfields, tens of authors and publications. Originally, however, it was the making of primarily a scholar, Ernst Haas. In fact, some scholars see in Haas’ work the inception of a separate field at the crossroads between international relations, economics and political science: European Integration studies (Rosamond, 2005). Haas’ Neofunctionalism, despite the assonance of names, carries fundamental differences from Mitrany’s work. First, Neofunctionalism, rather than a collection of normative principles, is a proper and testable theory which does not lack a comprehensive theoretical framework as its ancestor did. At least two volumes present a clear discussion of its theoretical bases: *The Uniting of Europe* (1958) for what concerns regional integration in Europe, and *Beyond the Nation State* (1964) presenting a functional theory of international relations on a global scale. Second, Haas attempts to provide systematic empirical tests of his theoretical prescriptions, which were

largely missing in Mitrany's work. Still, Neofunctionalism had been an evolving project as well: for instance, in 1975 already—when Haas' "quick federalization" predictions had clearly failed—the theory was "abandoned" by its own author (Haas, 1975), only to be rediscovered and expanded from 1986 onwards, when the integration process began once more, by Schmitter, Haas and others; a continuous opus of revision which lasted till Haas' last days, and concluded a long theoretical paper published few months after his death as an introduction to the 2004 re-edition of *The Uniting of Europe*.

Haas' Neofunctionalism analyses the process of supranational integration in two dimensions: a *macro* dimension, where the path-dependency and institutional logic of integration is assessed in its complexity, and a *micro* dimension, where the incentives and interests of individual actors is taken into account.

The *micro* dimension of Neofunctionalism (very much influenced by the "behavioural revolution" that American Political Science was experiencing at the time) is focused on individuals' and groups' incentives towards integration. Haas' agent theory may be labelled as "rational constructivism"; agents are *rational*, as they are aware of their own (economic, social) interests and act to maximise their payoffs; they are forward-looking, meaning that expectations play a key role in their demands; and their interests shift over time and respond, in a feedback process, to the evolution of the institutional environment in which they are embedded.<sup>4</sup> It follows that *National preferences*, instead of being exogenous variables determined by classical international relations' power games, are socially constructed through the interaction of the domestic community of interest groups. Agents' political loyalty, too, is socially constructed and depended on economic interests; the dependency of a group's utility on the existence of a given set of (eventually supranational) institutions would produce, over time, a shift of political loyalty towards those institutions.

In *macro* terms, Haas characterises the process of integration in two main phases: market integration (from trade liberalization to free movement of labour and capital) and political integration, which implies integration of fiscal and welfare policies (Haas 1958: 12-13). The connective link between then micro and the macro dimension of Neofunctionalism is the well-known process of spillover, now made explicit by Haas. Integration happens when it is welfare-improving: in other words, when it is output-legitimised.

---

<sup>4</sup>in his last work, published posthumous in 2004, Haas himself relabelled his agent theory as "soft rationality", as the forecasting capacities of political agents are limited and therefore unintended consequences are likely to emerge.



Therefore, dis-integration becomes increasingly unlikely as integration advances: the further down the process, the more likely that problems are resolved through further integration instead than through dismantlement of institutions. In a truly path-dependent fashion, formal, or “explicit” functions are complemented by “latent”, unintended functions which were not integrated originally but, following some sort of crisis, may be attributed to the new-born institutions (Haas, 1964; Merton, 1968). Such a competence accrual, however, is not automatic: it still requires a Sovereign agreement. A further coalition agreement is thus required, implying that further integration must be perceived as welfare-enhancing in all participating member states; periods of stagnation may emerge in the meantime. In Haas’ Neofunctionalism, therefore, *crises* play a double role: on the one hand, they work as a trigger of the spillover effect, letting latent functions to “emerge” and shifting agents’ preferences towards competence accrual; on the other hand, crises are the by-product of divergent interests across interest groups and national communities, and work as “brakes” applied to the integration process.

Despite the attempt to theorize breaks and slowdowns in the integration process, Haas expected a quick federalization process: trade integration would have required credit and currency integration, which in turn would have generated fiscal and political integration; “*this spill-over may make a political community in Europe in fact even before the end of the transitional period*” (Haas, 1958). Even if Haas’ Neofunctionalism implied “no specific temporal component” (Schmitter 2005: 257), the consequences of the long stagnation period between 1968 and 1986 were sharp for a theory that claimed to make testable conclusions and predicted a quick federalization pace; in fact, its failure and demise was acknowledged by Haas himself (1975). Also, original Neofunctionalism had no lack of shortcomings. First, it underestimated the role of national political leaders *as an interest group* in their own right, whose particular interest is to protect the competences and powers of the nation-states (intended as bureaucratic institutions) they represent; conversely, it overestimated the loyalty shift of other domestic interest groups. Second, the role of the Supranational bureaucracy, and of the Commission in particular, was excessively emphasized by Neofunctionalism, while the Commission acted, for most part, as a faithful agent of its national principals rather than as an autonomous political body seeking further expansion of its power. Third, the crisis-integration dynamics was largely left untheorized, despite being hinted at; only later work along with Schmitter (1969; 1970) attempted to address this issue, but in a moment when the body of key notions about

Neofunctionalism was already absorbed by scholarship, and criticism – fuelled by growing stagnation in the integration process—was on the rise. And finally, the possibility of a *geographical spillover*, and the consequent effects on the increased difficulty of achieving a “great bargain” (Scharpf, 1998) were largely neglected, although hinted at.

### 2.3. *Beyond Neofunctionalism: Schmitter's Neo-neofunctionalism*

When integration started again, following the 1986 Single European Act and the Treaties of Maastricht, Amsterdam and Nice, the idea that integration advances through major crises acquired new centrality. Many events had occurred however, in the meantime; since Haas' rebuttal of his own theory (Haas, 1975) two major crises had occurred; several treaties were signed; Europe had moved towards monetary integration and capital liberalization. Moreover, theories of European integration had flourished, enriched by contributions such as Moravcsik's liberal intergovernmentalism (Moravcsik, 1998) and “Multilevel Governance”. On the political spectrum, several referenda (both within the boundaries of the Now-European Union, like in France, Ireland and Denmark, or outside, like in Switzerland or Norway) had shown that the consensus towards European integration could no longer be taken for granted from citizens; furthermore, the Maastricht decision from the Bundesverfassungsgericht, and the debate on the missing “*Demos*” of the Union had brought the political discourse to challenge the political foundations of the process of integration. The idea that the Union could only be legitimised by its performance (Scharpf, 1970; 1998) was gaining ground. In this broad context, several authors (Schmitter (1969; 1970; 2002); Pierson, 1996; 2001) engage in a wide revision of the aging Neofunctionalist theory, providing a modern version of it endowed with a more complete, and therefore more nuanced vision of the integration process. This section presents Schmitter's Neo-neofunctionalism along with its complementary theory, Historical Institutionalism, as developed by Pierson (1996).

Schmitter's neo-Neofunctionalism is grounded in four key concepts: (i) *functional crises*; a complete version of the spilling process which I would label (ii) “*functional clock*”, (iii) *functional cycles*, and (iv) *functional equilibria*.<sup>5</sup> These concepts play a fundamental role in this dissertation: Chapter 2 deals with

---

<sup>5</sup> (a detailed description of the latter, as well as the reasons for its peculiar name, are provided in the opening pages of chapter 4).

the long-run visualization of functional cycles; Chapters 3 and 4 attempt to demonstrate that the Eurocrisis is a functional crisis, qualifying the nature of the spilling effect it generated over the functional clock; Chapters 5, 6 and 7 attempt to assess whether the crisis has produced a shift between functional cycles. It is therefore useful to recall these definitions at this stage of the theoretical introduction.

- (i) *Functional crises.* Neo-Neofunctionalism, more than any other previous versions, is a theory of crisis-led integration. In particular, it postulates that integration advances through cycles of functional crises. A functional crisis is characterised by two elements: first, it has, to some extent, *endogenous origins*; either directly, being the crisis generated by a precise failure of the previous allocation of competences to the supranational institutions, or indirectly, as the allocation of competences to the supranational institutions becomes suboptimal, or even unsustainable, due to changing environmental conditions (Schmitter, 2002). Chapter 3 attempts to demonstrate this point for the Eurocrisis. In both cases, the institutional setting is considered as in *functional disequilibrium*, meaning that the current allocation of competences is not sustainable for protracted periods of time.

Second, a functional crisis must be characterised by a *functional resolution*, meaning that its solution must involve a reallocation of competences across government layers; either through further integration (“spill-overs” and “spill-arounds”) or through re-nationalisation of competences (“spill back”); Chapter 4 deals with this issue for the Eurocrisis. This is due, of course, to the attempt (from national leaders and/or the supranational bureaucracy) to re-establish the capacity of the crisis-distressed functions to deliver. This in turn implies, if one thinks carefully, that integration advances when the *output legitimacy* (Scharpf, 1998) of the Union is low; the Union must have become somewhat dysfunctional for a pressure to reform it to emerge. Such a performance-drive progress, however, creates problems later on in the integration process, when the range of policies dealt at Supranational level include policies with widespread welfare effects, for instance fiscal policies. This issue is largely discussed in Chapters 5-7 of the dissertation.

- (ii) *The “functional clock”*. As Schmitter himself put it, any theory of integration should necessarily be also a theory of dis-integration (Schmitter, 1970; 2002; Schmitter and Lefkofridi, 2015a, 2015b). The simple “spillover”, as intended by early Neofunctionalists like Haas, is not sufficient to model the range of possible functional reactions to a crisis in terms of competences’ allocation. Therefore, additional concepts are introduced by Schmitter (1970). If spillover is defined as a simultaneous accrual of both the competences and the autonomy of supranational institutions, “*spill around*” means competences accrual within an intergovernmental framework; *spill-backs*, on the other hand, identify a decrease of competences and autonomy. Now, if competences and autonomy are identified as two crossed axes, then a fourth option emerges: “weak” spill-backs, whereby competences are decreased, but the remaining institutions are strengthened in their autonomy (Schmitter (1970), in a similar setting, refers to such options as “muddling-about”, although the meaning of the term has changed over time). The reaction following a functional crisis may go in any of these directions, depending on the conditions on the ground; chapter 4 offers a more detailed description of each of the options and of their underlying hypotheses, as well as a graphic visualization of the functional clock.
- (iii) *Functional cycles*. The third key concept of Neo-Neo functionalism that crises and integration are not randomly happening episodes; rather, they are interconnected through “functional cycles”. Each functional cycle, with the exception of the very first one, begins and ends with a functional crisis (Schmitter 2002:20); endogenous forces and path-dependency play a key role in all functional cycles with the exception of the first, where “endogenous conditions (...) and random variables play their most important role” (Schmitter, 2002:22). Initiating cycles, albeit hard to predict, are followed by “priming cycles”, characterised by an autonomous role of supranational bureaucracies and non-governmental actors seeking to expand the role of the “new centre”; priming cycles are therefore characterised by a tension towards spillovers. Finally, third and last are “transforming cycles”, where integration of the economies spills into “integration of politics” (Schmitter, 2002: 33). Transformative cycles are characterised by increased politicization on several levels: between member-states, on redistributive issues;

between centralised and national bureaucracies; between parties supporting integration, and parties opposing it. In other words, transformative cycles sign the beginning of a political struggle on the *finalité politique* of the Union, and will be mostly characterised by a deep political cleavage (almost in a Rokkan-Lipset (1967) fashion) between partisans of the “new centre” and of the “old periphery” (Etzioni, 2001).

- (iv) *Functional equilibria (encapsulation)*. Of course, integration is not a necessity: if a community of states manages to endure a functional crisis, or to solve it, without substantially re-allocating competences across layers of government (for example, by closure of external borders, changes in leaderships or in policies, or endure the pain and simply waiting for background conditions to change again) then the institutions would be considered “encapsulated” into a functional equilibrium. On the opposite direction, when inherent contradictions exist, then the system is in *functional disequilibrium*, which of course brings back the concept of crisis’ endogeneity discussed in the previous paragraphs. *If they existed*, Insulated Nation States would constitute institutions in functional equilibrium, where the four key functions of sovereignty (maintaining the well-established partition of Bodin (1576)) would be kept, generally, at the same level. Of course, being sovereignty (here, quite differently from Bodin) a divisible concept, supranational integration breaks the nation-state equilibrium. While some international organizations may succeed in finding a new equilibrium and being encapsulated early in the process of integration, the existence of a “gravitational attraction” of sovereignty – pulling the key sovereignty functions either towards complete integration, or towards renationalisation – cannot be ruled out a priori.<sup>6</sup> In other words, while encapsulation of international organizations is quite possible, theory suggests that, when integration concerns some (but not all) of the key functions of sovereignty, a pull towards either complete integration or renationalisation exists.

---

<sup>6</sup> Indeed, some scholars (for instance, Genschel and Jachtenfuchs (2016) have interpreted the recent crisis as a pull towards integration of remaining core state powers.

#### 2.4. Complementing Neo-neofunctionalism (1): Path-dependencies and the role of the State in Historical Institutionalism

Now, such a setting can explain the relationship between institutional change and crises only under two fundamental assumptions about agents' behavior: *bound rationality* and *socially-constructed preferences*. Endogenous crises are largely excluded by perfect rational choice approaches, which usually result in self-enforcing equilibrium models where unintended consequences are impossible; therefore, exogenous crises constitute the main vector of institutional change (Streeck and Thelen, 2005:7; Fioretos, 2011). To explain endogenous change, a nuanced version of rational decision making ("bound rationality", Haas, 1964; 2004) is required. Bound rationality does not imply that agents act irrationally, but that they are subject to all sources of imperfect information constraining the political agent's capacity of anticipating events, generating unforeseen consequences of decisions and, eventually, resulting in endogenous crises. Furthermore, both Neo-Neofunctionalism and historical institutionalism reject the notion of strictly exogenous preferences, which are instead assumed as (partially) unanchored and may change through distributional feedbacks, socialization processes and evolution of allegiances and identities (Haas, 1958; 1964; Pierson, 1996; Christiansen et al., 1999).

Haas' Neofunctionalism' had given –differently from more classical intergovernmentalist approaches— great emphasis to the role played by supranational decision-makers. However, as Pierson (1996) points out, in moments of supranational constitutional change ("*critical junctures*", as defined by Fabbrini (2015)) national decision-makers maintain a key role in shaping the outcomes of constitutional "grand-bargains". At this regard, intergovernmentalists (Keohane, 1984) and Neo-neofunctionalists (Schmitter, 1969;1970) agree that national decision-makers –even when confronted with endogenous crises— will generally set for the minimal concessions possible to address the outstanding problems, in the attempt to minimize the loss of national sovereignty in any given decisional cycle. Nonetheless, as the outcomes of each cycle influences the construction of preferences, the decisional mechanisms and even the shortcomings of the new institutional setting in itself, a one-point analysis of grand bargain episodes is largely insufficient to understand integration, as it would explain why the given decisions were agreed upon, but it would fail in

explaining why the necessity of taking such decisions had emerged in the first place; a long-term analytical perspective is instead required to understand in full the determinants of integration (Pierson, 1996: 126).

Both unforeseen consequences and socially-constructed preferences highlight the importance of path-dependency. Path-dependency, however, is a two-handed concept, as noted by Streeck and Thelen (2005: 6-7): it can be used both to explain institutional resilience to change in front of exogenous shocks (Pierson, 1996; Mahoney, 2000) *and* to explain endogenous change, dictated by the unforeseen consequences of previous steps of integration. Moreover, path-dependency-induced constraints explain the existence of institutional sub-optimal equilibria: the institutional solution given to a specific problem may be sub-optimal to fully address that problem, as it responds to a maximization logic which not only accounts for providing the ideal solution for the given problem, but also has to deal with legacy institutions “freezing” in rules (and when it comes to the EU, in treaties of constitutional nature) a previous composition of preferences.

Either way, crises are a recurrent explanation for institutional change. As discussed, Schmitter postulates-echoing, in that regard, policy-makers (Monnet, 1978; Prodi, 2001)- that integration advances through cycles of crises. The logic for this hypothesis is twofold. On the one hand (regardless of the limitations posed on the concept of rationality), crises render the status-quo unsustainable, generating the case for a re-allocation of competences towards a new equilibrium. Exogenous crises are more suited to explain change in settings approaching perfect rationality (Mahoney and Thelen, 2010: 6) where they tip the balance of pre-existing, self-enforcing institutional equilibria; Conversely, endogenous crises emerging from unforeseen consequences of previous cycles of integration are common in bound-rationality approaches (Haas, 2004).

Crises themselves can be induced, or facilitated, by incomplete integration. For once, economic integration in one field (let us say, monetary policy) may create the need for common policies in other fields (let us say, labour or fiscal policy) which, however, are not yet integrated; hence, the uncoordinated/divergent management at national level may then result in a crisis. More generally, if synergies between different “core” functions of sovereignty exist, partial integration of one of them may disrupt their internal coherency and generate instability and tension, ultimately resulting in either further integration of the remaining

functions, or towards renationalization of the previously integrated functions. In this regard, Genschel and Jachtenfruchs (2016) consider that as long as core state powers (money, economic policy, political representation, internal security and judicial administration) are maintained at a fundamentally separate level (in this case, national and supranational), a tension will persist between upward and downward shifts of competences.<sup>7</sup>

Crises and path-dependency are thus entangled. Path dependency can drive the emergence of sub-optimal, instable equilibria. Several factors contribute to this outcome: short-term decisional horizons, determined by electoral politics (Pierson, 1996: 135) imply higher social discount rates, and therefore less efficient long-term solutions; second, the resolution of a given crisis might not be the optimal one as achieving that result might entail the unfolding of previous agreements, which is often unfeasible (Scharpf, 1998); third, the marginal advantages of certain institutional settings may be not sufficiently high to off-set the costs of switching from an existing institutional set to a better one. Classical path-dependency (Pierson 1996) and Neofunctionalism (Schmitter, 1970; Schaprf, 1998) describe “lock-in” outcomes as the absence of significant institutional change in front of a crisis, as the costs of altering the status-quo in either direction are higher than the costs imposed by the crisis itself; path-dependency is therefore used to explain institutional resilience. In addition, even when national decision-makers might be tempted to recede from the existing agreements, the supranational bodies they institutionalized might use their authority to prevent such an outcome. However, the same outcome can be framed quite differently: a “lock-in” situation may emerge also because a crisis generates new distributional conflicts, and thus a divergence of preferences concerning the best resolution options; in that case, the absence of change is rather a sign of resilience or encapsulation.

---

<sup>7</sup> While Schmitter (1970; 2002) discusses, in his well-known “functional clock” of *spillover*, *spill-around*, *spill-backs*, the possibility of *encapsulation*, core functions of sovereignty are so naturally synergic that, when their supranational integration begins, they converge towards “final states of attraction”, either generating integration, or dis-integration.



### 2.5. Complementing Neo-neofunctionalism (2) Politicization and Postfunctionalism

From the analysis carried out in section 2.3, it should be evident that politicization, including *negative* politicization constructed through opposition to Europe (as contrasted to *positive* politicization through parliamentarization and identity-building, as suggested by Hix (Hix, et al. 2006; Hix, 2007, 2008; Hix and Noury, 2009) and Risse (2014), is definitively a possible outcome of Schmitter's Neo-Neofunctionalist model.<sup>8</sup>

Naturally, politicization is multi-faced phenomenon with several dimensions: *Polarization* of European issues indicates the increased divisiveness of issues related to European integration; Euroscepticism is thus interpreted as a rejection of increasing centralization (Hix, 2007) which creates a new social cleavage *à la* Rokkan-Lipset (Nicolini, 2014); *Salience* captures the relative importance of European issues in respect to other elements of public life; *autonomy* indicates the strengthening of the freedom of action of Supranational executive bodies in respect to the national governments, which entails the creation of a supranational political sphere; and *parlamentarization* indicates the strengthening of the role of the European Parliament in the decision-making process. Increased politicization of the process of European integration may entail increases in one or more of these different dimensions of politicization. The politicization of a Neo-Neofunctionalist dynamics, which constitutes the engine of Schmitter's "transforming cycles", becomes a central feature of Hooghe and Marks' (2008) "Postfunctionalism", who emphasize, however, its *negative* character – i.e. relying, especially, on increased salience and polarization. In other words, provided that the non-politicized phase of European integration was characterized by a

---

<sup>8</sup> Negative politicization was expected by other Neofunctionalist scholars too: Early Neofunctionalist theorists expected a surge of nationalism against the process of centralization as a phenomenon characterising the fourth and conclusive phase of integration of a federal state, when the ruling groups are engaged to proceed with political integration (Haas, 1964); the absence of solidarity and common nationhood among the countries of the Union implies that central institutions cannot be based on truly democratic values. Instead, central institutions are likely to acquire an authoritarian nature in the attempt to perform central government functions without having the necessary democratic backstop. As a reaction, "traditional nationalism" would emerge in the nation states, where dissident units try to regain their autonomy achieving secession. In Haas' vision, the federation can be saved only by the establishment of a shared "liberal nationalism", where common values and norms are built over time among the different units. The issue of secession from the process of integration is discussed also by Etzioni (2001: 95); the units opposing integration face a choice between –on one side– "taking over" the central institutions, either from within the political process or through a revolution, and –on the other side– pursuing a secession from the system. In the author's views, the final choice is determined by the level of integration achieved by the Union when the opposition gains momentum: the more the different polities of the Union are integrated, the more an endogenous change will be likely in respect to secession (Etzioni 2001: 314).

“permissive consensus” (Hooghe and Marks, 2009), increased polarization necessarily implies the rise of dissensus towards integration.

While some have interpreted Hooghe-Marks’ Postfunctionalism as a rejection of functionalism (for instance, Schimmelfennig 2014), I maintain that Postfunctionalism is rather an interpretation of the “reality” of negative politicization, as expected by Neo-Neofunctionalism; Postfunctionalism, in other words, is treated here as the study of a particular configuration of politicization, the latter expected in Neofunctionalism itself. As the European Union moves beyond the purely pro-market organization it used to be at its inception, the existence of “policies without politics” (Schmidt, 2006: 223) becomes increasingly unsustainable. In other words, “*The end of the market Honeymoon*” (De Witte & Hartmann, 2013) increases the likelihood of the emergence—in the absence of a classical majority-opposition dynamics—of forms of *opposition to the system* instead of *opposition in the system*, the latter characterising national democracies (Castelli Gattinara & Froio, 2014). Addressing the collapse of output legitimacy (to use Scharpf’s (1998) interpretation of Easton) constituted the engine of Neofunctional integration during crisis-initiated priming cycles, when the Union’s competences were largely regulative (Majone, 1998; 2012). However, as the Union grows beyond purely regulative functions, the solution of output legitimacy crises entails, to some extent, input-legitimacy crises, and the ensuing negative politicization (the first part of Chapter 5 describes with great detail, including a few graphical visualizations, this switch from Neofunctional, output-led integration towards Postfunctional, input-led integration).

A further specification is needed here. Following Majone (1998), regulative institutions (such as the pre-crisis European Union) perform better when “insulated”, i.e. when they are maintained isolated from the political cycle of the member-states. In a crisis, when—by definition— output legitimacy is low, *elites* seek to address the crisis by re-establishing the effectiveness of integration, eventually through further integration. However, when the crisis requires integration of redistributive policies, both input and output legitimacy are needed; if an agreement on mechanisms to provide input legitimacy cannot be forged, is likely that output legitimacy will remain low (again, these issues are widely discussed in chapter 5). In sum, two main channels of functionally-generated, negative politicization are identified:

- (i) *Contestability deficit.* In the simplest (yet least attractive) case, if no solutions are in place and the democratic deficit is not addressed, negative politicization would increase as direct consequence the persistence of democratic deficit; it is therefore likely to affect most dimensions of politicization (with the exception, perhaps, of *autonomy*). One shall note that, when it comes to redistributive policies, it is rather complex to achieve the horizontal effectiveness required to obtain output legitimacy, as discussed in the second part of Chapter 5. Input legitimacy is therefore needed to ensure that the redistributive policies in place can be contested and changed to the benefit of the largest possible majority. It follows that, if no democratic institutions are in place, introducing a Europeanized redistributive policy may entail a twin-deficit on both input and output side, driven by the lack of opportunities for contestability and change of the policies in place. Through this channel, negative politicization would be pushed forward both by parties asking for full democratization of the EU (“Euroreformism”), and by parties asking for a change in policy orientation (“soft Euroscepticism”).
- (ii) *Identity cleavage.* Negative politicization cannot be ruled out even if appropriate democratic institutions are put in place. On the one hand, as extensively discussed in Nicoli (2014), even if appropriate representative institutions are in place (i.e., increase *parlamentarization* of the Union is achieved), the persistent lack of common identity of the Europeans (the notorious “no-demos” hypothesis) may fuel nationalistic resentment and strengthen the national cleavages, both in the parliamentary process and in the increased *salience* of European issues in national press. Moreover, even if appropriate institutions are in place and a sense of common identity emerges in large shares of the European population, some negative politicization may be due to the simple transferring of competences towards a central institution, therefore entailing a “centre-periphery” cleavage on the issue of sovereignty. Through this channel, negative politicization would be pushed forward by parties opposing the EU as concept, relying on nationalistic or economic arguments (“hard Euroscepticism”).

In sum, increased negative politicization seems hard to avoid when integration “spills” from its Neofunctional, priming cycle to its Postfunctional, transformative cycle; it will be either be fuelled by a

lack of contestability (affecting the “losers” of the new redistributive policies), or by a lack of shared identity (widening the identity cleavage), or by defendants of national sovereignty (widening the centre-periphery cleavage), in any combination. While the Neofunctional phase of integration (characterised by a performance deficit, as discussed in Chapter 5) could easily produce a build-up of the common institutions and policies, the introduction of redistributive policies will be met with opposition certain groups no matter how democratic the institutions introduced will be. To be successful, the Postfunctional dynamics of integration—despite being led by democratic deficit—requires not only the creation of common democratic institutions, but also a growing sense of common identity and some degree of allegiance to a “new centre” (Etzioni, 2001). Without these conditions, integration will be countered by widespread opposition.

### 3. Operationalising Contemporary Functionalism

As shown in the previous section, Contemporary Functionalism builds upon a variety of insights. From it borrows its crisis theory (and relative outcomes) from Neo-neofunctionalism; it borrows path-dependency and unforeseen consequences from historical institutionalism; and it borrows politicization dynamics from Postfunctionalism.

As stated earlier in the introduction, this dissertation aims to solve a two-tier research problem. First, it aims to establish whether the Eurocrisis can be considered a *functional crisis*, adopting Schmitter’s definition; second, it aims to assess the extent the Eurocrisis is politicizing the process of European Integration, and therefore can be considered as the inception moment of a transforming cycle. The two research questions, albeit strictly linked, are qualitatively different: the first one, by determining if the Eurocrisis is indeed a functional crisis, aims to assess whether it is *appropriate* to apply a neo-Neofunctional model; the second question, by analyzing crisis-induced politicization, aims to assess whether the Eurocrisis constitutes the beginning of a *transforming cycle*: meaning that it aims to assess a particular set of predictions of the model.

Before discussing the research questions of this dissertation and their operationalization, Section 3 provides a short summary of definitions and assumptions of neo-Neofunctionalism, as adopted here. In particular, it discusses the dimensions, the micro-assumptions, and the macro-assumptions of the model.

### 3.1. The dimensions of the model

Contemporary functionalism is a complex theoretical toolbox for analyzing integration. The model may be fine-tuned over two dimensions: a micro/macro dimension (Schmitter, 2002), and a normal times/crisis times dimension (Fabbrini, 2015). Depending on the combination of dimensions, different processes and agents become primary objects of research.

*The micro/macro dimension* identifies the level of the neo-Neofunctional analysis: a micro focus requires to analyze agents' behavior and preferences; a macro focus requires to consider crises in their systemic nature, therefore looking to macrosocial and macroeconomic dynamics. The “normal times”/“crisis times” dimension identifies the environmental, background conditions of integration; “normal times” neo-Neofunctionalism assesses how single policy fields, for which competences have been already attributed, at least to some extent, to an international organization, evolve over time due to endogenous and exogenous pressures; “normal times” Neo-Neofunctionalism, therefore, implies no change to primary law. “Crisis times” Neo-Neofunctionalism assesses how major crises affect the overall distribution of competences especially (although not exclusively) through primary law, including treaty creation and revision. Depending on the combination of these two dimensions, the object of study may change (table 1).

Table 1 The dimensions of Neo-Neofunctionalism	<i>Micro analysis</i>	<i>Macro analysis</i>
<i>Normal times</i>	Individuals, group preferences within give policy fields; their role in shaping policies over time. The <i>national</i> dimension of preferences retains lower importance in respect to crisis-time functionalism; supranational bureaucracies and interest groups are relatively more important.	The mechanism through which the spilling process advances within already-attributed competences
<i>Crisis times</i>	The channels and extent individual and group preferences are affected by major crises; how they concur in the formation of national bargaining positions; how individual and group preferences set the agenda for Treaty Reform; National bureaucracies and interest groups are relatively more important.	The mechanism through which crises are endogenously generated; the systemic bottlenecks and contradictions which create the conditions for a crisis-led spilling process to emerge.

Dealing with a disruptive event such as the Eurocrisis, this doctoral dissertation focuses especially on both micro- and macro-functionalism in crisis times; on the macro dimension, (Chapters 3, 6 and the first part of Chapter 4) the focus is on the national economies and societies, as well as on the Union as a whole; on

the micro dimension (Second part of Chapter 4 and Chapter 7) the focus is on institutions and parties. One should note that the fundamental difference between Neofunctionalism and Institutionalism- namely that in the former agents determine the structure, while the opposite is true in the latter is greatly weakened in Contemporary Functionalism. While agents maintain their decisional autonomy, not only their rationality is limited, but their option sets are constrained by path-dependency.

### 3.2. *The model's macro-assumptions*

Most of the macro-assumptions of the model, i.e. the structure and key features of the model itself, are derived from Schmitter and have been already described extensively in the previous section. A common assumption to all versions of functionalism concerns (1) the nature of sovereignty:

Sovereignty is *divisible* in its essential functions, some of which may be transferred, temporarily or permanently, to other agents or institutions. Moreover, sovereignty is substantial in nature, i.e. belonging to those that practically exert it, instead than formal, i.e. belonging to those who maintain the ultimate legal power of deciding.<sup>9</sup> Although controversial, such a substantial definition of sovereignty is required because the exercise of ultimate, formal sovereignty may entail costs that the agents entitled with such a power are never willing to accept.

Furthermore, building on Schmitter's theory, the model assumes that (2) integration advances through *functional crises*; that (3) *functional crises* generate, and conclude, *decision-making cycles*; that (4) the reaction to a functional crisis can be qualified over the two dimensions (competences and governance) of the *functional clock*; and that (5) when crises do not generate further integration or disintegration but are successfully addressed without re-allocation of competences, the institution is in *functional equilibrium*.

### 3.3. *The model's micro- assumptions.*

---

<sup>9</sup> As discussed above, following Bodin's classification, the key functions of sovereignty are defense, external borders, justice, and currency issuance.

All functionalist and Neofunctionalist approaches share a set of common micro-assumptions, although their relative emphasis varies across versions of the theory; they are widely used throughout this dissertation.

They concern *delegation*, *rationality* and *interests*.

- (i) Given the macro-assumption about the divisibility of sovereignty, it follows that *delegation chains* may be weak: citizens, organized in a plethora of interest groups (parties, business associations, ONGs) have preferences and interests that can be (weakly) transmitted to their agents: national bureaucracies and governments (whose accountability is however limited); in turn, national governments exert a (weak) control over their own agents, the inter-national bureaucracies and government. Both national and inter-national bureaucracies, therefore, exist as agents (pushing forward their principals' agendas) but also as their own principals with their own set of interests and preferences; it results in a nested model where some agents/principals maximize their own payoff while keeping their own principals' payoff sufficiently high (given the strength of the controlling chain). Of course, different decisional settings attribute different decisional powers to different actors: while interest groups may play a direct role in day-to-day policy making of a supranational institution, their role is more indirect when new competences are to be transferred by means of a new Treaty, whereby the role of national governments becomes key (Fabbrini, 2015)
- (ii) Third, all actors (national groups, international groups' coalitions, national bureaucracies, international bureaucracies) are endowed with a *soft rationality* (Haas, 2004); meaning that (generally) integration happens only when agents have rationally assessed benefits and possible problems from integration itself, although (a) mistakes in assessment may exist over time, and (b) the actors' capacity of understanding completely the long-term implications of their decisions is to some extent blurred; as a result, *unintended consequences* of integration may arise. This is due to two fundamental reasons: firstly, because –by definition – the future is uncertain, and therefore both endogenous and exogenous shocks are hard to predict; and-
- (iii) -secondly, because actors' *interests* and *preferences* are socially and historically constructed: they are in part endogenous to the process of integration itself, which entails negotiation,

learning and socialization processes. This is true at all levels: for individuals, for groups (including national bureaucracies) and for “states” as a whole.

- (iv) Finally, following Scharpf (1998) and Majone (1998; 2012) the model assumes that a positive preference for integration requires that the expected integration will be input-legitimized if redistributive in nature, and output-legitimised if regulative in nature (this issue is widely discussed in the first sections of Chapter 5).

Combining together the micro- and macro- assumptions of the model it is possible to obtain a dynamic model built upon a set of four main relationships. First (A) the model expects that the *change in competences distribution between national and supranational level* (institutional accrual) is a function of (a1) the intensity of the crisis, (a2) the agents’ preferences for integration, and (a3) other exogenous factors. In turn (B) the *intensity of the crisis* is a function of (b1) the contradictions inherent in the distribution of competences in the previous cycle, (or “functional disequilibrium”), (b2) the steps recently undertaken to address them (i.e., short term institutional accrual), (b3) domestic factors specific to each geographical unit, and (b4) exogenous shocks (both symmetric and asymmetric). Third (C), the preferences of agents towards integration are a function of (c1) their expected gains and losses from changes in the distribution of competences, (c2) the intensity of the crisis, (c3) their inherent ideology towards more/less cosmopolitan solutions (i.e., their level of nationalism), and (c4) the degree of input legitimacy expected, given the redistributive nature of the function expected.

Now, let’s recall that politicization is a multi-dimensional phenomenon, constituted by four key elements: polarization (and thus, opposition); salience, parliamentarization, and autonomy (see previous section). Crisis intensity affects all four elements, although through different channels. In general, (D) the *change in the degree of politicization* of the supranational tier of government is a function of (d1) the extent the expected policies have distributional effects, (d2) the intensity of the crisis, (d3) the features of the decision making process, (d4) the degree of “Europeanized” identity of voters (i.e., the opposite of their level of nationalism), and (d5) other effects. Of course, different combinations of these elements may yield very different outcomes in the *kind* of politicization. For example, a particularly strong crisis, combined with a strong national identity, is likely to increase polarization/opposition; on the other hand, policies with



redistributive effects, combined with a rather Europeanized identity of voters, may result in a strong preference for autonomy and parlamentarization (the identity issue is widely discussed in Chapter 5 as well as in Nicoli (2015), a complementary work to this doctoral dissertation).

### 3.4 Questions and associated hypotheses

Naturally, a general test of the model is beyond the purpose and means of this dissertation. As stated earlier in the introduction, the goal of this dissertation is twofold: on the one hand, assessing whether contemporary functionalism is appropriate as an analytical framework to study the integration effects of the Eurocrisis; second, it aims to assess whether crisis-induced politicization, if present, is sufficient to consider that a *transforming cycle* has been triggered, implying, ultimately, either the transformation of the EU in a sovereign political entity, or otherwise its demise. This twofold research problem is thus split into two wide research questions: (Research Question 1) *Is the Eurocrisis a functional crisis?* and (Research Question 2) *has the Eurocrisis triggered a transformative cycle?*

Providing an answer to the first Research Question requires the testing of two distinct hypotheses, addressing, respectively, the relationships A and B of the previous paragraph. In particular, assessing whether the *Eurocrisis is a functional crisis* requires verifying that:

*H.1a- endogeneity.* Following relationship B, as well as the definition of Functional Crisis provided in section 2.3, *the direct or indirect endogeneity of the crisis must be assessed*; in other words, to be qualified as a functional crisis, *the Eurocrisis must be the result of a functional disequilibrium of direct or indirect origin.*<sup>10</sup>

*H.1b- functional resolution.* Following both relationships, A and B, as well as the definition of Functional Crisis be provided in section 2.3, the resolution to the crisis itself must be associated with a change in the allocation of competences, either through further integration (spillover, spill-around) or through disintegration (spill-back).

---

<sup>10</sup> "indirect endogeneity" implies that, even if a shock is external, its resolution is not possible because of the lacking functions of the European Union. As discussed in Chapter 3, several economic theories provide divergent views of whether the EU was (and is) really lacking competences or not. From the point of view of this analysis, however, we are not interested in confirming one theory or the other (although the analysis might show that certain actions have been more effective). Rather we aim to demonstrate whether indeed were institutional and competences shortcomings that prevented crisis resolution.

Providing an answer to the second Research Question also requires the testing of several hypotheses, related to relationships A, B, C and D. In particular, assessing whether the Eurocrisis has triggered a transformative cycle requires verifying that:

*H.2a- preferences.* The Eurocrisis has shifted preferences upwards for integration in fields which entail a high level of politicization (“core state powers”), meaning that the preferences mentioned in relationship a2 concern policies and institutions whose integration would require input legitimacy (thereby generating either parliamentarization or opposition to the EU).

*h.2b- opposition.* In absence of fully input-legitimized institutions, failure in addressing the crisis undermines the output legitimacy of the Union, therefore generating widespread opposition (relationship d2).

### *3.5 Operationalisation of the hypotheses.*

The four hypotheses of the dissertation, two concerning the functional nature of the crisis, and two concerning the ensuing politicization, are discussed through the six, largely stand-alone papers composing the thesis’ Chapters (A comprehensive summary of the thesis’ operationalization through the chapters was presented in Table A in the last pages of the Introduction).

Part One of the dissertation deals with the first broad research question: “*is the Eurocrisis a functional crisis?*” Chapter Two does not directly contribute to the answer of this question, however. Rather, it provides a long-term historical overview of European Integration as a sequence of institutional decisions shaped by functionally-linked crises. It provides an innovative reading of the path-dependency and of the connections between Europe’s multiple crises from the 1960s till today, and it works largely as second, historical introduction to the thesis. As a stand-alone paper, the Chapter is currently in review at the *Journal of Common Market Studies*.

Chapter Three tests Hypothesis *H.1a*, concerning the *endogeneity* of the Eurocrisis. In order to do so, it firstly provides an extensive literature review on the origins of the crisis, to establish which factors are to be considered as endogenous in their effects to the crisis, and what factors are instead of exogenous (purely imported, or purely domestic) origins. The section reconstructs a theoretical framework which illustrates

the determinants of the crisis, as well the limitations of the EU institutions in dealing with the crisis. At this regard, the relationships between full and partial endogeneity, as well as crisis resolution outcomes, discussed in *H1a* and *H1b* require better specification:

- (1) If an endogenous crisis is solved without a re-arrangement of competences, the Union has successfully encapsulated its crisis.
- (2) If an exogenous crisis is solved without a re-arrangement of competences, then the crisis is question it is not a functional crisis as defined in this work.
- (3) if a crisis (endogenous or exogenous) is not solved, but one of the survey theories prescribes that it would be solved if the competences were re-arranged, then the judgement must be suspended.
- It follows that (4) backward induction is adopted in the case of “partially endogenous” crises. In fact, if the crisis was exogenous in its origins, but the reallocation of competences solved it, then it was (in fact) partially endogenous, because if those competences were differently organised in the first place, reaction (2) would have happened instead.

More in detail, to verify *H.1a*, a composite index of Crisis Intensity is created from data concerning both financial distress (the 10 years yield on public bonds as reported monthly by the ECB) and social distress (the unemployment rate). The indicator is used as a dependent variable on a set of panel regressions covering quarterly data from 2008 to 2014, for a total of well over 700 observations. In the attempt to establish a degree of endogeneity of the crisis, the goal of the study is twofold: on the one hand, it attempts to find evidence of the role of variables described by the literature as provoking inherent contradictions within monetary unions. On the other hand, from a more macro perspective, it attempts to assess (through both separate and pooled regressions) whether those variables have had a stronger impact for Monetary Union countries, rather than for non-monetary union ones. As a stand-alone paper, the empirical analysis carried out there is being prepared for a special issue published by the *INET Working Group on European Political Economy*.

Chapter Four deals with hypothesis *H.1b*, concerning the functional resolution of the crisis. Naturally, it is self-evident that the Eurocrisis has generated several new policies and institutions; the paper, therefore, examines qualitatively whether the various institutions created in the wake of the Eurocrisis fit into the

specific hypotheses concerning *spillover*, *spill-arounds* and *spill-backs*. The second part of the paper conducts an in-depth analysis of the cases of *spillover* of the European Commission, discussing whether the crisis-generated institutions have also contributed to strengthen the Commission's *autonomy*, therefore providing early elements of politicization. As a stand-alone paper, the Chapter is currently under review at the *Journal of European Integration*.

Chapter Five is a largely theoretical undertaking, developing further the concept of functional legitimacy and setting the debate for the following two chapters. In particular, the chapter shows how a theory of legitimacy (and of the lack thereof) is needed in order to understand the switch from a Neofunctional mode of integration (led by performance deficits) to a Postfunctional mode of integration (led by democratic deficits). The second part of the chapter shows that the Eurocrisis, and its resolution, presents all the characteristics for such a change to emerge; the third part of the chapter discusses the ensuing legitimacy trilemma. The paper exists in three stand-alone versions which emphasize different elements. An earlier version is published as a Chapter in the volume "*Europe's Crisis: The Conflict-Theoretical Perspective*" (2015). A second version, with strong emphasis on the trilemma and its resolution, is in final review at the *Journal of European Integration*. A third version, composed by the first part of the paper and parts of this Introduction, develops further the concept of *Functional Legitimacy* for the *Polish Journal of Political Science*. In general, Chapter Four works as a further theoretical introduction for the second part of the paper, dealing with the second research question "*has the Eurocrisis triggered a transformative cycle?*"

Chapter Six deals with *H.2a* concerning the effect of the crisis on *preferences*. A custom database, hand-crafted (not without pain) through merging of nine rounds of Eurobarometer data, captures the evolution of citizens' preference on a range of different options for fiscal integration. Three indicators are so obtained: an index of preferences for fiscal integration, preferences for Eurobonds, and opinions concerning whether the EU does have sufficient powers to address the crisis. *H.2a* is then tested through panel data analysis on the three Dependent Variables. The stand-alone version of the paper is not yet under review, but is planned to be submitted in October for the journal *European Union Politics*.

Finally, chapter Seven deals with *H.2b* concerning the effect of the crisis on *opposition to Europe*. The paper deals with the notion of Hard-Line (or Extreme) Euroscepticism. It collects data of the electoral

performance of all Hard-Line Eurosceptic Parties in the EU with more than 1% of the vote sharing, for all elections of national and European relevance occurred in the EU since 2008 (for a total of 108 elections). A set of panel regressions is the run to assess whether the crisis, and the institutions that have ensued, have contributed to the rise of Hard-Line Eurosceptic parties. The stand-alone version of the paper has been accepted for publication on the *Journal of Common Market Studies*.



## Chapter Two: Crises and institutional change the long-run: an historical overview of Europe's 70 years of unintended integration.

### Abstract

Does integration advance through crises, as hinted by functionalist theorists and by policy-makers such as Jean Monnet or Romano Prodi? This paper provides a coherent understanding of the economic logic of European integration from its very inception to today's challenges, with a specific focus on periods of crisis, in the attempt of showing how each incremental step in integration constituted a response to a specific macroeconomic challenge. Three specific phases of integration are identified, each marked by a fundamental challenge visualized by a trilemma; the response on one specific set of problems resolves one given crisis, but sets the stage for the next set of problems to arise. The "Single Market Trilemma", or (Meade's trilemma), characterized the then-EEC from 1958 to 1986; the "Monetary Trilemma" characterized the EU between 1986 and 1999; and the "legitimacy trilemma" has applied since 2011 and it is yet to be resolved.

Note: a shortened version of this paper has been submitted and it is now in second review at the *Review of International Political Economy*.





# **Crises and institutional change in the long-run: an historical overview of Europe's 70 years of unintended integration.**

## **1. Introduction**

The process of European integration has been both accused of, and praised for relying mostly on economic factors. The importance of economic integration in the building-up of the European Union should not be understated, although it hardly constitutes the only relevant component of European integration. Against this background, this paper offers a coherent understanding of the economic logic of European integration from its very inception to today's challenges, with a specific focus on periods of crisis inherited from both the Neofunctionalist paradigm and Fabbrini's (2015) "critical junctures" approach. Since the seminal work of Mitrany (1919/1975), Haas (1958), and Balassa (1961) there has been a growing debate on the economic drivers of European integration. Policy-makers have often shared the view that economic crises shape the process of integration and constitute occasions for addressing the shortcomings of the existing institutions.

Since Schmitter (1970), functionalist theory has assumed integration advances through crises, and –as long as the political system under observation is in a state of functional disequilibrium— crises are shaped by incomplete integration. In this regard, Genschel and Jachtenfruchs (2016) consider that as long as core state powers (monetary, judicial and military powers, and the ensuing budgetary functions) are

maintained at a fundamentally separate level (in this case, national and supranational), a tension will persist between upward and downward shifts of competences. This paper focuses on the economic dynamics that

have led European integration. Haas (1958) studied in detail the functional logic that led to the build-up of the then European Economic Community (EEC); this paper reconstructs a stylized interpretation of the process of integration since then by showing how each incremental step in integration constituted a response to a specific macroeconomic challenge. The paper is composed of five sections: Section 2 investigates the general idea of crisis-induced integration; Section 3 discusses the first “pseudo-trilemma” and the creation of the Single Market; Section 4 analyses the second trilemma and the creation of the Monetary Union; Section 5 concludes by examining the still-unsolved third “pseudo-trilemma” of political integration.<sup>1</sup> It must be noted that this paper explicitly focuses on the post- Rome treaty period for two main reasons. First, the functional dynamics that led the original Steel and Carbon communities to build-up into the Rom Treaty is already very well covered by Haas (1958). Second, as specified in Chapter 1, we build upon Schmitter’s Neo-neofunctionalist approach, according to which “initiating cycles” (to which the Rome treaty belongs), by definition cannot have endogenous origins and therefore are rarely induced by endogenous crises, which emerge as a consequence of partial prior integration. “Priming” and “Transforming” cycles, instead, are determined by the shortcomings of prior phases of integration, and therefore are consisted with a crisis-based analysis as the one carried over in this Chapter. Also, it is worth noting that we focus especially on economic crises not because -from a theoretical standpoint- only economic crises matter. Rather, as the Union concerned, primarily, economic functions and institutions, it is more likely that the crises that emerge by those institutions’ incompleteness are mostly of economic nature. Functional spillovers into fields of complete non-economic nature, however, is not excluded ex-ante, as discussed towards the end of the chapter.

## **2. Crisis-induced integration: an overview**

Does integration advance through crises, as hinted by Jean Monnet and Romano Prodi, and to what extent are crises intrinsic to European integration? The crisis affecting Europe since 2010 constitutes an interesting

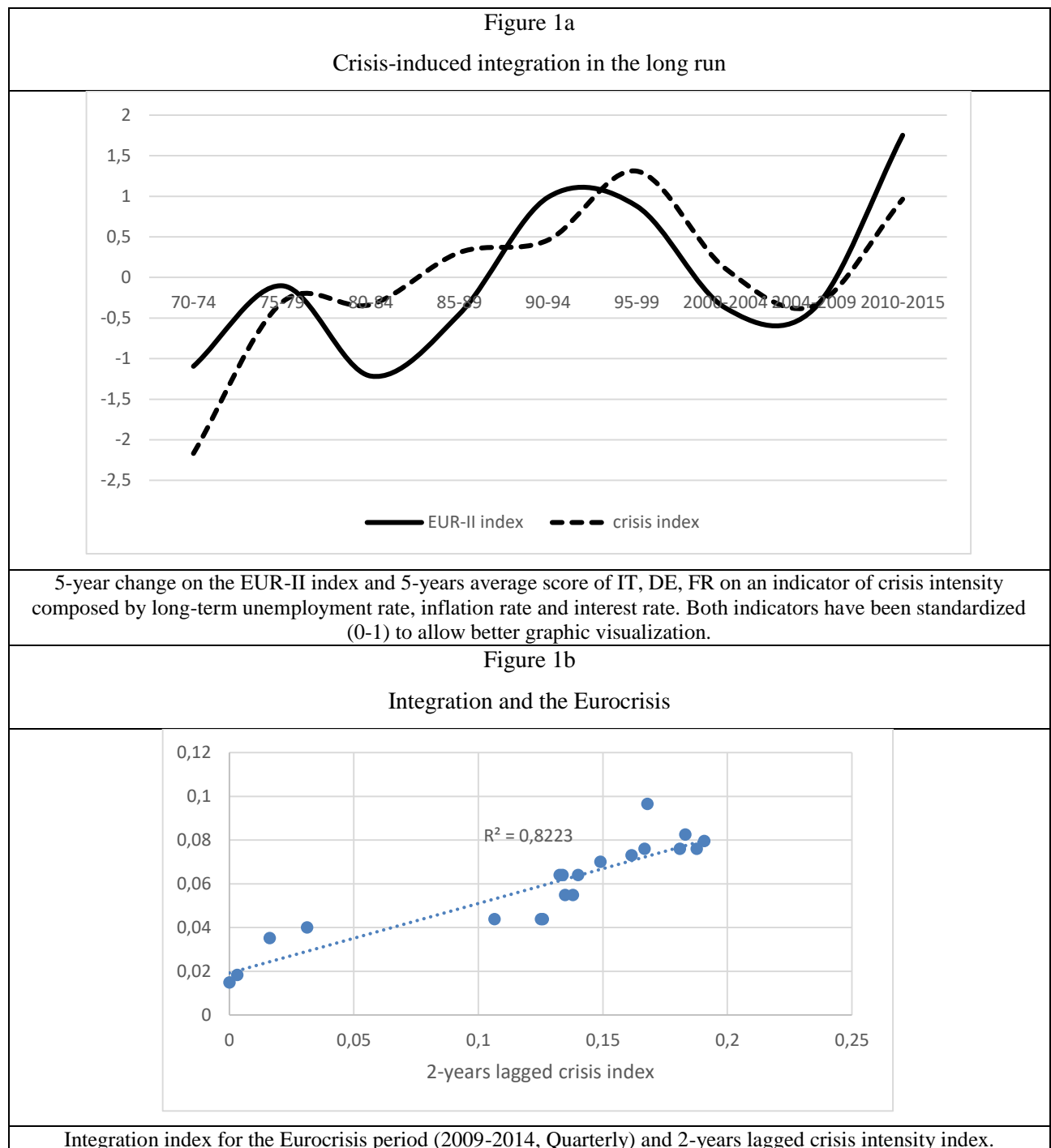
---

<sup>1</sup> Trilemmas and pseudo-trilemmas are similar but differentiated tools. The logic of a trilemma is mathematical, whereas the logic of a pseudo-trilemma is political. A trilemma implies the logical impossibility of keeping the three vertexes together; violating this boundary condition would result in immediate crisis. Psudo-trilemmas do not imply a logical impossibility, but the features included in the vertexes would create economic and political tension over time if they remain unaddressed. Violating a trilemma would result in sudden crisis; violating a pseudo-trilemma would first result in prolonged stagnation and tension in the process of integration, which would hinder performance and capacity of addressing problems and may result in a dis-integrative crisis.

testbed for verifying the functional hypothesis on the relationship between crisis and integration. The next Chapters attempt to provide a specific answer to this question, while Niemann and Ioannou (2015) show that the crisis-led integration that has occurred since 2011 constitutes a case of neo-functionalism. It is still unclear, however, to what extent such a relationship holds in the long run, and whether a theoretically tenable argument can be made. This paper argues that European integration can be read a sequence of responses to precise economic challenges, which, as long as they remain unaddressed, produce periods of crisis. In this regard, Figure 1 shows the long-term relationship between the 5-year average of the European Regional Integration Index, developed by the ECB (Dorucci et al. 2015) and the 5-year average of a crisis-intensity indicator (based on long-term unemployment), from the late 1960s to 2015. The correlation coefficient between the two indicators is about 0.75, suggesting that some degree of interdependence exists. During periods of distress (Figure 1b for the Eurocrisis) correlation coefficients are even higher. Far from proving any causality, this descriptive evidence suggests that the two processes are somewhat related. Modern functionalism postulates that if a causation link exists, it should be bi-directional: functional integration is a response to a crisis environment, while the crisis, in turn, may depend on incomplete (functional) integration achieved in the past, specifically because its incomplete nature can both be a source of instability and render the existing institutions less able to deal with new challenges (Schmitter, 2002).

An effective way of understanding Europe's economic integration is to visualize it a series of responses to sequential trilemmas and pseudo-trilemmas. Trilemmas hold the advantage of combining together information on both the fundamental challenges of integration and the inherent costs associated with their practical solution; thus they are able to explain protracted periods of "muddling-through". Examples of narratives of European integration based on trilemmas have appeared before: Fahri and Werning (2012) and Dymski (2013) attempt to apply Mundell (1961; 1963) trilemma to the EU case; several studies have interpreted late stages of European integration following Rodrik's (2007; 2011) trilemma, either with direct transposition (Damonte, 2008; Crum, 2013; Snell, 2016) or with substantial changes to the trilemma logic (see Chapter 5 of this dissertation, as well as Nicoli 2015). However, little has been done to reconstruct a coherent pattern based on consequential trilemmas. Two attempts have been made: O'Rourke (2011) describes the process of European integration as the response to two sequential trilemmas, while Strauss-

Kahn (2012) presents the EU as particular institutional setting producing a response to three simultaneous trilemmas.



This paper provides instead a different perspective, proposing a three-stage process of integration. The trilemma-led logic of economic integration is clearly of functional origins: the response on one specific set of problems resolves one given crisis, but sets the stage for the next set of problems to arise. I identify three

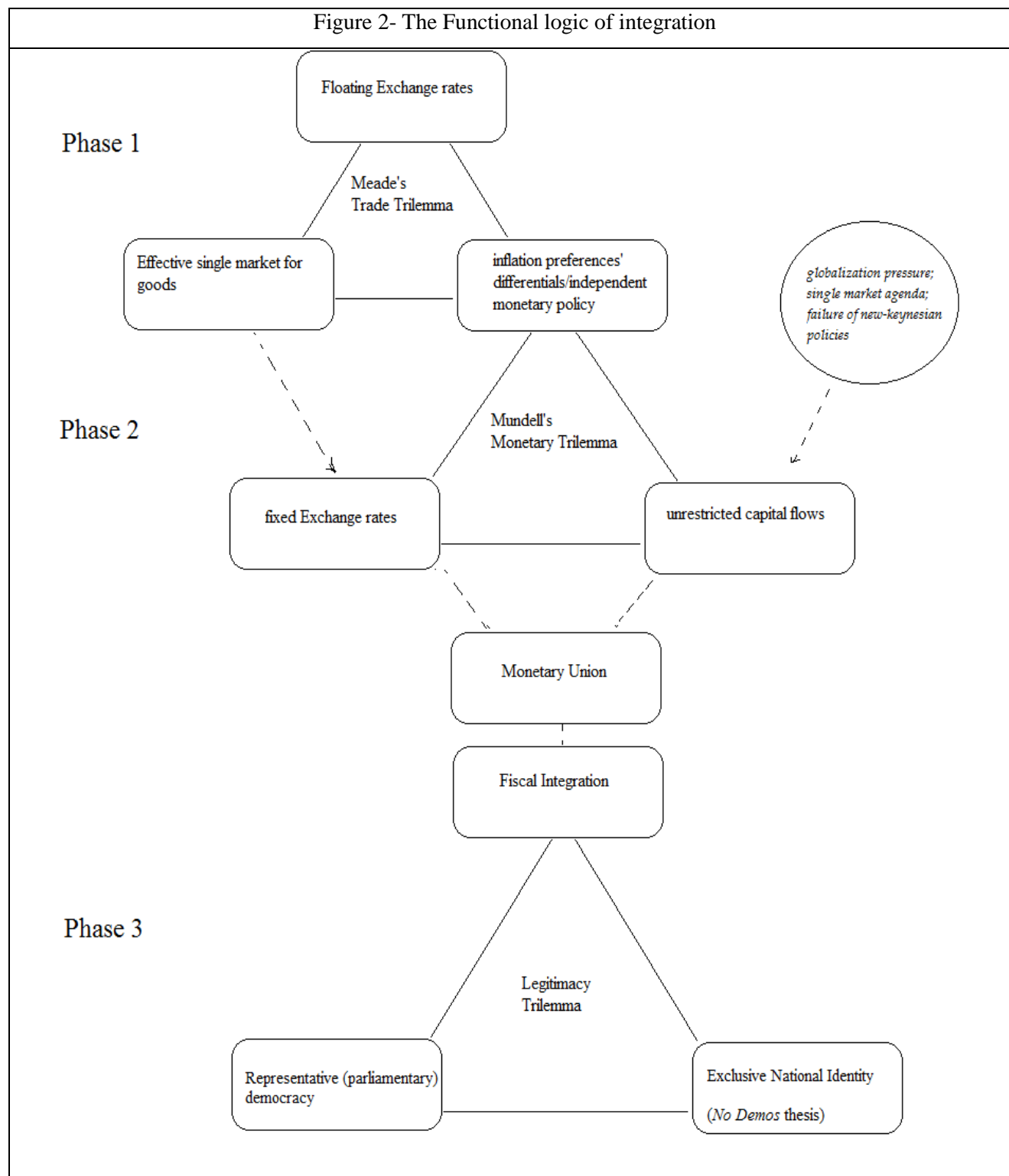
specific phases of integration, each marked by a fundamental challenge visualized by a trilemma. The “Single Market Trilemma”, or (Meade’s pseudo-trilemma), characterized the then-EEC from 1958 to 1985; the “Monetary Trilemma” characterized the EU between 1986 and 1999; and the “legitimacy pseudo-trilemma” has applied since 2011 and it is yet to be resolved. Each of the next sections addresses the fundamental challenges of one given period, discussing how it relates with the previous and the following ones.

### **3. Phase 1: The Common Market Challenge and Meade’s pseudo-trilemma**

In 1958 the then-six countries that created the Coal and Steel Community reached an agreement on the creation of a common market without internal barriers that was to be implemented by 1967. At the time few believed they would have succeeded (Fauri, 2006). The creation of the EEC was the result of several previous failed attempts to create a stable framework for economic and political integration that had exposed the reciprocal mistrust still lurking among the European nations. Monnet’s solution to proceed with sectorial, limited integration aimed to neutralize the widespread opposition to larger, more ambitious plans for political integration. The source of this opposition was mainly found, according to Monnet, in nationalistic resentment; the shadow of the war was yet to disappear (Olivi, 2000). However, some doubted the viability of the project from an economic point of view as well; for instance, Meade (Nobel prize for economics in 1977) showed that “full free trade agreements” were costly to maintain between countries with different economic preferences without having to renounce to more than the power of setting external tariffs (Meade, 1957). Although Meade himself never formalized a proper pseudo-trilemma, his reasoning is better understood in such a configuration (Figure 2-phase 1). In absence of trade barriers between countries, Meade noted that monetary policy could become a strong instrument to enact “beggar-thy-neighbor” strategies if the Central Bank of a country decides to have an explicit exchange rate target and adapts monetary policy accordingly. With the power of establishing trade barriers still in the hand of national policy-makers, any attempt to adopt a competitive devaluation of one currency versus another could be matched either by (i) an equal depreciation, or (ii) by a rise in the external tariffs, or (iii) by means of wage moderation and internal devaluation. A tic-for-tac response on monetary policy, however, is not always suitable: European countries have, in fact, different preferences concerning optimal inflation rates.

Since inflation is a well-known byproduct of protracted competitive depreciation strategies, countries with lower tolerance for inflation would be more willing to react to a partner's competitive depreciation with a rise in tariffs rather than a similar response in monetary policy.

Figure 2- The Functional logic of integration



Clearly, introducing a common market would remove option No. (ii), the possibility of recurring to external tariffs to protect domestic employment (Meade, 1957; McKinnon, 1973:3). Therefore, in front of competitive devaluation enacted by a trade partner, lower inflation countries are left with no good choices: either they give in, depreciating the currency as well (option No.(i)) and therefore accepting a higher inflation rate than the national optimal; or they proceed with internal wage moderation (iii) to maintain a non-monetary competitive edge<sup>2</sup>. Alternatively, they must accept a higher unemployment rate than desired, and the loss of market shares to the depreciating country (at least in the short term).

In low-inflation countries, none of these choices is politically easy to adopt and each could provoke a political reaction, potentially leading to the emergence of a majority against the free-trade agreement (in the absence of which trade barriers could be raised to face the partner's external depreciation). Naturally, competitive depreciations can be prevented through some kind of fixed-exchange agreement (under which devaluations are prohibited). a pseudo-trilemma ensues, in which floating exchange rate (which allows devaluations), an effective single market (which prevents trade barriers), and different inflation preferences cannot simultaneously coexist.

In principle, a pseudo-trilemma would make any decision very costly and complex to achieve, since agents are unwilling to give up any of the options. Economic instability, and potentially economic crisis is – in its endogenous component – dependent also on this inability to take a credible decision.

Any conclusion based on Meade's pseudo-trilemma may look, *prima facie*, at odds with reality: the emergence of the EEC was neither marked by extremely long negotiations nor by periods of economic crisis. The Rome Treaty was conceived in 1955 at the Messina Conference, prepared through the Spaak Report in 1956 and discussed in Venice the same year, and finally signed and ratified by the six members in Rome in 1957; it entered into force the following year. While the original agreement included a transition phase of at least 12 years for the complete removal of trade barriers (Treaty of Rome, Art. 8), the process

---

<sup>2</sup> Naturally, we are assuming here that competition happens primarily on the costs side, instead on the quality side. Whilst this clearly constitutes a simplification which does not fully capture reality, it is also important to notice that relative prices are a variable that public power can, directly or indirectly, influence; product innovation and quality is likely out of the public power's reach (in most, although probably not all cases).

was already completed by late 1967 – i.e. three years before schedule – and the transitional measures ceased to be in force as of July 1968. The political success of the EEC was complemented by its constitutionalisation by the European Court of Justice (ECJ), which in two cases – *Van Gend en Loos*, 1962, and *Costa v. Enel*, 1964 – introduced the fundamental principles of primacy and direct effect of EEC regulations.

Two main reasons contributed to the smooth success of the operation. On the one hand, the period of sustained economic growth that accompanied the implementation of the treaty constituted the optimal environment for taking decisions with potential long run economic costs. On the other hand, many observers failed to acknowledge that, in fact, the first pseudo-trilemma was already solved even before the creation of the EEC: Europe had been in a system of semi-fixed exchange rates since the end of the war thanks to the Bretton Woods system and to the European Monetary Agreement, which from 1958 onwards maintained the European currencies within a quasi-fixed fluctuation band of  $\pm 0.75\%$ . There was no pseudo-trilemma-induced tension in the negotiations leading to the EEC or during its implementation period because there was no pseudo-trilemma standing any longer: a solution (quasi-fixed exchange rates) was already in place before the negotiations on the EEC had even begun, and Europe only had to bank on it by removing trade barriers. As long as the Bretton Woods system held, differentials in inflation preferences and the ensuing “beggar-thy-neighbor” monetary policies were no threat to the Common Market.

With the collapse of Bretton Woods and the two oil shocks, the inherent tensions within the common market emerged. The divergent responses in fiscal and monetary policy to the oil shocks by Germany and the Netherlands, on the one hand, and France and Italy, on the other, lead to further monetary instability (Fauri 2006). The sudden increase in oil prices also put the manufacturing sectors of European countries under stress since energy, a key factor of production, became more expensive; as a result, Europe experienced a simultaneous rise in inflation and unemployment which altered the domestic preferences concerning trade barriers across the EEC (Schirm, 2002). As suggested by Meade, the divergent monetary policies started to put the common market in danger (McKinnon, 1973:3). This pressure on the common market induced a series of efforts for closer monetary cooperation which begun with a Commission memorandum in 1969



about monetary integration, leading to the release of the Werner Report (Werner, 1970). While the report also acknowledged the impact of monetary divergence on the common market, it stated that capital flow liberalization had to proceed along with monetary coordination, and therefore simple fixed exchange rate mechanisms were insufficient. The report called for full monetary and fiscal integration by 1986, but was largely ignored by European policy-makers, who were mostly concentrated on finding domestic solutions to the crisis (Fauri, 2006). The attempt to reproduce a Europeanised version of Bretton Woods, albeit with looser fluctuation bands, was launched in 1972 at an intergovernmental conference in Basel, but went under stress within a year; by 1974 only Germany, Denmark, and the Benelux countries managed to maintain their commitments to the system.

One of the leading reasons for the failure was indeed monetary and economic policy divergence in face of the oil shocks and the ensuing rise of both inflation and unemployment. In the attempt to maintain the full employment achieved at the end of the 1960s, Italy, France and the UK loosened their monetary stance letting inflation increase, in the belief that –following the Phillips curve— a trade-off between low inflation and low unemployment is always in place. The ensuing waves of currency devaluations put the Common Market under stress; nonetheless, while the divergence of monetary policies exposed the full extent of the trade-offs between a common market and domestic employment objectives, currency devaluations were accompanied by other forms of resurging protectionism. Although the Treaty of Rome explicitly prohibited intra-EEC tariffs and quantitative restrictions to the import of goods, the participants attempted to find alternative measures “of equivalent effect” to quantitative restrictions, most often in the form of technical regulations. Moreover, the reliance of several states on large, public-held corporations undermined free competition in those countries, as public operators enjoyed regulatory, fiscal and monetary protection from their masters. In this environment of growing rejection of free competition, the ECJ was forced to act in the defence of the Common Market: the two landmark cases of the 1970s –*Dassonville*,<sup>8</sup> 1974, and *Cassis de Dijon*, 1979 – enforced the principle of free circulation of goods even in cases of measures with effects equivalent to import restrictions.

Nevertheless, the trilemma’s fundamental contradiction could not be solved by the ECJ. To address the monetary side of the problem, by 1979 a new monetary coordination accord was agreed: the European

Monetary System and its Exchange Rate Mechanism (ERM) was launched in 1979 and allowed for a maximal fluctuation of 4.5%. To achieve this goal, joint action to hedge speculative attacks was envisaged by all participating central banks once a currency was approaching the lower/upper threshold. With monetary policy constrained by the new agreement and regulative protectionism blocked by the ECJ activism, the newly-elected socialist government of France, the centre-left governments of Italy, and the Labour government of the UK had only one arrow left to deliver on their electoral goal of full employment—public spending. The economic programme of François Mitterrand in the years 1981-1984 is the most representative of this approach: in this period, public debt increased from 9.1% of GDP in 1980 to 17.6%; spending on assistance social security increased from 22.6% of GDP to 25%; the minimum wage was increased by almost 40% from 1981 to 1982 alone; nationalized industrial complex increased from 5% to 8% of GDP from 1981 to 1982, and concerned 90% of the French banking system (Sachs & Wyplosz, 1986).

Mitterrand's plans and similar (although less ambitious) action plans taken by Italy and, previously, the UK fell short of expectations. The French growth rate from 1981 to 1983 averaged only 1% per year, while inflation peaked at the decade-high score of 12.6% in 1982. Worse, huge capital outflows occurred, putting the French Franc under heavy pressure and causing several devaluations (Sachs & Wyplosz, 1986: 276). One of the leading reasons behind the failure of this early phase of Mitterrand's economic policy was a misjudgment of the evolving global economy. The world economy in the early 1980s was much different from the "golden age" of the new Keynesian policies of the 1960s and the early 1970s: in particular, globalization was rising at an increasing pace and capitals were becoming much more mobile on a global scale, decreasing the effectiveness of domestic spending plans (Schirm, 2002). In such a framework, the French government failed to acknowledge that –lacking the domestic supply sector competitiveness-- an increase in public spending would have resulted mostly in increased inflow of foreign goods and in an ensuing capital outflow. Moreover, Mitterrand's policies were perceived as highly punitive for the business community, leading to a draining of investment, reduced economic activity, and reinforcing the capital outflow; by the end of 1983, globalization had won the match and the French government was obliged to switch its policy-mix completely. The "*Tournant de la Rigueur*" from late 1983 onwards, marked the second phase of Mitterrand's economic policy, including easing labour regulations, inflation control,

decrease in public spending, and — after an initial tightening of capital controls (Sachs & Wyplosz, 1986:293)— capital flows liberalization. The latter had come to be seen as a condition for success in the “new” globalized world. From 1983 onwards, Jacques Delors, previously the Economics Minister of Mitterand’s government, added budget and finance to his portfolio; with Delors in the driving seat of the French economy, the priorities of the European countries, including the Conservative Government of the UK that had been in power since 1979, started to align towards a pro-market liberalization agenda, opening a window of opportunity for a comprehensive reform of the EEC. Delors became President of the Commission in January 1985 and released the White Paper on the Single Market by June that year, calling for full mobility of capital, labour, and services (alongside goods) within the Community.

Under Mitterand/Delors leadership, the French economy slowly bowed towards stability, despite two more devaluations in July 1985 and April 1986. By 1986, the second phase of the European Monetary System, which included domestic interest rate coordination, was introduced (Mongelli 2008:12). Given that changes in money supply will impact the exchange rate, regardless of the nominal commitment that a central bank could have concerning its defense, a fixed exchange rate system is not really a fixed exchange rate system if central banks fail to coordinate their interest rates (hence, aligning their inflationary preferences, consistently with the Meade’s trilemma expectations which predicted that either fixed exchange rates or different preferences over inflation should disappear were the Single Market be functional).<sup>3</sup> Furthermore, from an economic perspective, completing the internal market was finally recognized as the only way to move beyond the 1970s stagflation and the early 1980s failures of Keynesian policy-making; as assessed by the ECJ in the 1984 *Luisi-Carbone* decision, restrictions to capital mobility constituted one of the main obstacles to that goal. A revised Treaty – the Single European Act (SEA) – was agreed in December 1985 and approved by all member-states by February 1986; it entered into force in July 1987. The SEA aimed specifically to remove the limitations of the Single Market, including barriers to capital mobility and technical regulations.

---

<sup>3</sup> From this point of view, the EMS became a real fixed exchange rate regime only when the Central Banks decided to cooperate in setting the interest rate in 1986, when EMS Phase 2 was introduced along with the SEA Treaty. Furthermore, the IMF (1988: 48-56) show that the EMS, despite not solving the community monetary problems of its own before 1986, produced a substantial deflationary pressure which helped realigning the currencies from 1986 onwards.

#### **4. Phase 2: Europe under Mundell's Trilemma**

The approval of the SEA, coupled with renewed efforts to ensure Central Banks' independence across Europe, succeeded in improving the ERM's credibility. The formal end of capital controls, envisaged in the SEA, was due to several pressures: on the one hand, the liberalization agenda of Thatcher and Delors, and the pressure of globalization which threatened to render Europe unattractive for global investment if controls were to remain in place (Schirm, 2002); on the other hand, the French need for leveraging the Single Market as the only solution left to boost domestic employment, provided that monetary policy was heavily constrained by the increasing Independence of Banque de France and the ERM commitment. The consequence of liberalizing capital flows, however, escalated the monetary problem (Ludlow, 2013:18); the first stage of European integration- the Common Market era, from 1958 to 1986- ended with the Single European Act and the establishment of the Single Market in 1993. The critical problem of the first stage of integration, which occurred after the collapse of Bretton Woods, was never really solved; Meade's pseudo-trilemma was never properly addressed and the inherent tensions within the common market caused by devaluations never disappeared. Without capital controls, simple fixed exchange rate mechanisms, upon which the European Monetary System was built, would become untenable: a new, proper trilemma had arisen.

The theoretical underpinning of the new trilemma was developed by Mundell (1960; 1961) although it is unclear who used the term first after Mundell's seminal work. The logic of the trilemma is clear: there cannot be simultaneously free capital mobility, fixed exchange rates, and independent monetary policy. In case of full capital mobility, any divergence in monetary policies across countries would spell the end of the fixed exchange rate regime (Figure 2-phase 2). After the entrance into force of the Single European Act, the EEC found itself precisely in this situation: a fixed exchange rate regime was needed to prevent free-riding in the Common Market setting, as explained in the previous section (left arrow in Figure 2-phase 2), and free capital mobility was required to complete the Common Market into the Single Market, which was a requirement to maintain Europe's stance in a globalized world and the only policy option left after the failure of new-Keynesian policies in the 1970s and 1980s.

The solution of Mundell's Trilemma for fixed exchange rates and unrestricted capital flows, however, is not costless: it requires the participating countries to give up independent monetary policy— i.e., to create an “irrevocably fixed exchange rate” in the form of a proper Monetary Union with a common Central Bank (De Grauwe, 2007). Any other form of agreement would not be sufficiently credible, as shown by the failure of both the ERM and of Europe's “Monetary Snake”; regardless of the commitments undertaken at European level, independent central banks would have faced, at some point, a situation in which committing reserves to defend the exchange rate would only deplete them without altering the final result. Therefore, abandoning the defense of the exchange rate would have been the optimal choice since the beginning; knowing that, international speculators had simply to stage an appropriately sized financial attack to trigger devaluation (Obstfeld, 1986; 1996).

The simple logic of these “self-fulfilling crises” rendered any monetary agreement different from a full-fledged currency union as not credible in the long run. By the time the Single European Act was agreed, the issue was becoming increasingly clear: the end of capitals controls would spell doom for the ERM, which succeeded in stabilizing the participants' exchange rates between 1984 and 1992. To prevent monetary instability from re-emerging and putting the Single Market under stress once again – a problem identified by the Padoa Schioppa Report in 1987 (Ludlow, 2013:18) – the European Commission relaunched the idea of a three-stage monetary unification originally proposed by Werner in 1970; the 1989 Delors Report called for a three-stage monetary union to be achieved by the end of the century. The first stage of the Monetary Union – full liberalization of capital movements – was indeed launched in 1990, but by then the European Governments were already deeply into talks about a new treaty. Negotiations for a full-fledged new treaty were determined by the need for a leap forward not only in monetary integration but in all aspects affected by the establishment of a functioning Single Market for goods, services and capitals by 1992, such as mobility of people. Other “spillover effects” of the Single European Act were in fact inducing EEC leaders to expand the community fields of action not only into monetary affairs for the reasons discussed, but also in Justice and Home affairs, which would have been clearly affected by freedom of circulation and the disappearance of border controls (Ludlow, 2013:21). The end of the Cold War and the German reunification accelerated, but did not determine, the process of codifying a new treaty with a

clear political goal: the transformation of the European Communities first into the European Community and then in the European Union (Loth, 2013).

The core of the discussions concerning the Maastricht treaty were not focused on the establishment of a Monetary Union, but on the political structure to support it. It is important to note that, while monetary integration was perceived as a requirement to address the currency instability that had marked the previous two decades, fiscal and economic policy was not. As Fabbrini (2015) observe, the rules-based coordination of fiscal policies laid down in the Maastricht Treaty was, from this point of view, only a great compromise between the French will to maintain national sovereignty in this policy field and the German supranational approach; while monetary integration became a fully supranational policy, fiscal and economic policies became matters of intergovernmental coordination.

The Single Market for goods and capitals, complemented by a monetary union and freedom of movements, were finally codified in the Treaty of Maastricht at the end of 1991. Once the second stage of the EMU was to begin, at some point in the mid-1990s, convergence of fiscal and monetary policies would have been introduced in order to lay ground for the final stage. The full Monetary Union, however, was to be established only as a third, ultimate phase of the process, while capital mobility was effectively introduced by July 1990. As a consequence, the unstable nature of the European Monetary System's ERM emerged again. The specific episode identified by the literature (see Buiter, Corsetti & Pesenti, 1998, for a summary) as the occasion for the system's implosion was the tightening of German monetary policy due to post-reunification capital inflows and public investment, which were driving inflation up. The other ERM countries could not follow the Bundesbank's lead in monetary tightening and a crisis ensued. In 20 days of September 1992 the Italian Lira and the British Pound were obliged to devalue to such an extent that they had to leave the ERM; the Spanish Peso depreciated by more than 5%, and all other ERM currencies were close to the lower limit of their band (Buiter, Corsetti & Pesenti, 1998:24). Further attacks followed by the end of the year against Spain and Portugal and continued for the large part of 1993. The Franc succeeded in remaining in the ERM, although at the very bottom of the band, only thanks to a costly intervention from the Bundesbank and to a reduction of the German interest rate. The "old" system with 4.5% fluctuation

bands, was definitively abandoned in spring 1993 and replaced with a quasi-flexible exchange rate agreement with fluctuation bands of 15% around the central parity (30% in total).

Proceeding further towards monetary integration, transiting to the second stage, was now a priority to protect the Single Market from further monetary instability; stage 2 of the EMU, implying convergence around the well-known “Maastricht criteria” and fiscal consolidation, was agreed to begin by 1<sup>st</sup> of January 1994. In November 1993 regulation 3605/93 was passed, introducing the first form of fiscal coordination that would evolve into the Stability and Growth Pact four years later; regulation 3604/93 strengthened the principle of Central banks’ independence and prohibition of monetary financing embodied in article 104 of the Maastricht Treaty; the European Monetary Institute (EMI) – a support body and a forum of discussion for central banks – was launched on January 1<sup>st</sup>, 1994; the Euro as a currency name was formally adopted in December 1995. With the launch of the second stage of the EMU the convergence criteria laid down in the Treaty of Maastricht started to apply, forcing national governments interested in joining the Euro to maintain a stable exchange rate and to curb inflation, deficit, and debt. Concerning the latter two, as an application of the provisions of the Treaty on an Excessive Deficit Procedure, regulations 1466/1997 and 1467/1997 – the so-called Stability and Growth Pact – were introduced. In the same year, the EMI presented the design of the new currency notes, and a new Exchange Rate Mechanism (ERM-II) was agreed to deal with exchange rates between Euro adopters and the other countries. The domestic political effort behind the convergence process in EMU stage 2 was generally perceived as serious: both domestic agents and international financial markets were aware of Europe’s need for a permanent solution delivering monetary stability (De Grauwe, 2007). The final list of 11 early Euro adopters was agreed in 1998, along with the “permanently fixed exchange rates”; the new currency was introduced as soon as January 1999, only 6 years after the collapse of the ERM.<sup>4</sup> In a way, the quest for a stable solution to the Mundell trilemma was

---

<sup>4</sup> The lack of speculative attacks on the converging currencies has, to some extent, puzzled observers, who have wondered why a definitively fixed parity has succeeded where a more flexible adjustable rate had been crushed in less than a month. The explanation offered by De Grauwe, (2007) (among others), is twofold: on the one hand, a monetary union, once implemented, is much more resilient to financial attacks precisely because it removes domestic monetary incentives; on the other hand, the political effort invested in the process between 1994 and 1998 was so large in all member-states that the mutual insurance from central banks to defend the “permanently fixed” parities between 1998 and 1999 was indeed credible.

self-fulfilling as well: as soon as the effort became sufficiently serious and the prospect of actual monetary integration in Europe became more and more realistic, the fixed exchange rate system that the Single Market so much needed became more credible and so did the common guarantee from Central Banks to preserve the agreed parities (De Grauwe, 2007), pulling financial markets' expectations along.

### **5. Phase 3: The Eurocrisis and the issue of legitimacy**

The Euro was introduced on 1 January 1999 for 11 countries. Despite an initial dip in its exchange rate with the US Dollar, it quickly rose to the second place among the world's reserve currencies. The adoption of the process contributed to the impressive convergence of interest rates and (in a lesser extent) of inflation rates of the participating member states: the spread between the 10-year Italian bond and the equivalent German Bund was 800 basis points in 1993, it decreased to 200 basis points by 1997 and was virtually zero by 2001; the spread between the Bund and the 10-year Greek bond moved from 1750 basis points in 1993 to less than 50 in 2001. Compared with other policy areas of European integration, the first ten years of the EMU were almost eventless. While the 2000s were intense years for European integration (the Amsterdam Treaty in 1997, the Nice Treaty in 2001, the failed Constitutional Treaty in 2005, the two enlargements in 2004 and 2007), the life of the Currency Union appeared, on the surface, smooth and resilient. The infamous warning of the then President of the European Commission, Romano Prodi, during an interview with the *Financial Times*<sup>5</sup> went almost unnoticed. The economic and fiscal coordination elements of the EMU, the former embodied in the so-called "Open Method of Coordination", the latter in the Stability and Growth Pact, not only remained in the exclusive field of intergovernmental cooperation, but their effectiveness in constraining domestic behavior was watered down in 2003, when the Council vetoed the opening of an Excessive Deficit Procedure against France and Germany; the supervisory powers of the Commission were formally decreased in the 2005 revision of the SGP, rendering any action against non-compliant member states politically implausible.

---

<sup>5</sup> ("I am sure the euro will oblige us to introduce a new set of economic policy instruments. It is politically impossible to propose them now, but some day there will be a crisis and new instruments will be created"- Prodi, 2001)



Since Kenen's (1969) application of Mundell (1960, 1961) it is well-known that a Currency Union without a high degree of factors mobility and price flexibility, coupled with the absence of a centralised budget and of a lender of last resort would have been particularly weak when experiencing economic shocks, especially when the shocks are asymmetric or when the capacity of enacting countermeasures differ. The need to complement monetary integration with a degree of fiscal integration was well known in Brussels. It was discussed as a conclusive phase of the Werner Plan in 1970, it featured as key element of the McDougall Report (McDougall, 1977), and it was discussed by both the Padoa-Schioppa Report in 1988 and the Delors Report the year after. However, fiscal integration was left out of the Maastricht Treaty mostly to appease Mitterrand's fears on losses of national sovereignty (Loth, 2013); fears that were, to some extent, corroborated by the French referendum in 1992 which narrowly approved the new Treaty with a 51% majority. Moreover, a formal limitation to supranational fiscal integration was set up by the 1993 "solange" decision on the Maastricht Treaty delivered by the German Bundesverfassungsgericht; according to the Court, the EU was lacking sufficient democratic legitimacy to be considered as democratic on its own, thus any decision with redistributive effects would be in line with the German constitution only "as long as" the German Parliament maintained the final word on it. The same theoretical framework was then reiterated by the Court's 2009 "*Lisbon*" decision, and by the 2013 "*ESM*" decision. In general, the cold reaction to Maastricht has been described as the end of "permissive consensus" on European integration and the beginning of a "restrictive dissensus" (Hooghe & Marks, 2009); a new phase of "post-functional" European integration characterized by increased Euroscepticism and mass involvement.

The EMU, therefore, was introduced only with very limited fiscal backstops. The only element of fiscal integration was the intergovernmental Stability and Growth Pact; no enforceable economic policy coordination was expected<sup>6</sup>, no banking union was envisaged, no lender of last resort was set up, nor was a shock-absorption mechanism. It was hoped, however, that the EMU would be "endogenously optimal" (De Grauwe & Mongelli, 2005): the simple process of monetary integration would have triggered a process of convergence, decreasing the likelihood of asymmetric shocks. While it was clearly so for interest rates and, partially, for inflation rates, the endogenous convergence process was much less pronounced in other

---

<sup>6</sup> After 2000, labour and economic policies were to be loosely coordinated through the "Open Method of Coordination", which failed, however, to produce any form of sensible convergence (ECB, 2013)

fields, such as labour costs, where the performance between Germany (which enacted strong salary moderation from 2003 onwards) and peripheral countries substantially diverged (De Grauwe, 2012); in turn, labour costs divergence hindered earlier inflation convergence. Also, some have even suggested that monetary integration may increase specialization of national economies, thus increasing divergence in business cycles as sector-specific shocks become country-specific shocks (Krugman, 1995). The issue of convergence/divergence in the EMU generated a lively debate both in theory and empirical studies (see next chapter for a summary). If the EMU showed that it could not cope with divergence and asymmetric crises, some forms of centralised government would have been needed; as Mundell himself put it, “it will be achieved because, for Europe, it isn't just the best game in town, it's the only game” (Wallace, 2006). As a matter of fact, when the global financial crisis erupted in the US, the EMU was a substantially less homogeneous economy than what was originally thought. The connection between the global crisis and the Eurocrisis has been widely discussed in the literature, and a general consensus between leading economists has emerged, pointing to a series of root-causes of the crisis (Baldwin et al., 2015). In particular, increase of private debt, unsupervised banking sector and its connection with public finances, divergence in labour costs, and lack of appropriate EMU institutions (such as a proper lender of last resort and a European stabilization budget) have been pointed out (Baldwin et al., 2015).

As is well known, the Eurocrisis produced an unprecedented wave of integration in fiscal and economic policy. Not only the 2005 version of the SGP was revised, substantially increasing the powers of the European Commission; a new fiscal treaty (the Treaty on Stability, Coordination and Governance-TSCG) was signed, building the legal bases for stronger supervision of domestic finances; three lending institutions, including the permanent European Stability Mechanism, were established; the first two pillars of a Banking Union (Common Supervision of large banks and common resolution framework) have been created; and the Open Method of Coordination has been overhauled into the European Semester, a much more intrusive- albeit not yet justiciable- procedure of economic policy coordination. Finally, a fundamental change in the ECB's own interpretation of its mandate has provided the EMU with a lender of last resort since the 2012 speech of Mario Draghi and the introduction of the OMT programme. While still lacking its own budget and a full-fledged banking union, the EMU is committed to evolve further towards a fiscal federation by 2025, as outlined in the 2015 Five Presidents' Report (Juncker, 2015).

Despite progress, however, the crisis is yet to be fully solved, and resentment against the perceived responsibility of the Euro is growing (see Chapter 7 of this dissertation, also published as Nicoli, 2016). A fundamental conundrum remains still: if the EMU is to evolve into some kind of fiscal federation, as it is already beginning to do, how is it to be legitimized? This problem calls into question the very foundations of European constitutional order. As Fabbrini (2015) notes, the EU has been a project based on two constitutional pillars of supranationalism and intergovernmentalism, both reflected in the double constitution of the Maastricht Treaty. In economic policy, this tension was embedded by the French and German struggle over economic governance during the Maastricht negotiations, and emphasized by several decisions of the Bundesverfassungsgericht (*Maastricht*, 1993; *Lisbon*, 2009).

Indeed, the dilemma is even more profound, because, when redistributive policies are concerned, supranational insulation (Majone, 1997) is no longer possible and democratic oversight is required (Majone, 2013). Democratic decision making on fiscal and economic policy has been stressed by constitutional courts, not least by the Bundesverfassungsgericht that, in its 2009 Lisbon decision, put fiscal policy among the fundamental competences having to remain under parliamentary control if democracy is to be maintained (Bvg, 2009:252). Yet, the European Parliament, or any other pan-European parliamentary assembly, might not be entitled to acquire such powers: such transfers of power would entail the establishment of EMU-wide redistributive policies, which require a degree of solidarity (and thus, of shared identity) among European people which many argue is yet to emerge. Proponents of the so-called “no-demos” thesis argue that the Europeans are not “a people” and shall not become one, since this would entail the creation of a common identity; but as long as there is no European *demos*, no majority voting (and thus, democracy) is possible; any fiscal policy would have to be dealt with in a pure intergovernmental framework. A third functional pseudo-trilemma of economic integration is thus dictated by the need of fiscal integration, the requirement of democratic decision making, and the lack of common identity (figure 2-phase 3).

While this last pseudo-trilemma may loosely recall Rodrik (2007) and Crum (2013), two fundamental differences exist: first, not *any* degree of integration triggers the need for democratic decision making, but only integration of redistributive policies (Majone 1997; 2013); in other words, the Eurocrisis pushes the

EMU in the last pseudo-trilemma through the need for fiscal integration. Second, *nation states* do not constitute –like in Rodrik’s– a *vertex* of the pseudo-trilemma; they rather constitute *the historical solution* of the pseudo-trilemma –for democracy and fiscal integration- on a given area. The fundamental third pillar concerns, broadly, the lack of a common identity, which is a condition for democratically-governed redistributive policies (Weiler, 2001); a nation state, when it is grounded in some degree of common identity, is a solution to the pseudo-trilemma; when common identity lacks, nation states become threatened.<sup>7</sup>

## 6. Conclusions: Convergence of economies or convergence of identities?

In the aim of substantiating the adage that “integration advances through crises”, this Chapter has presented a comprehensive and coherent reading of crisis-led integration in Europe, enshrined in a series of nested trilemmas. The third functional pseudo-trilemma yet to be resolved, and –if the Five Presidents Report is to be believed– it won’t be addressed until 2025, almost 70 years after the Treaty of Rome. As long as it is not addressed, the Eurocrisis—and related democratic dissatisfaction with the state of the EU—will not disappear. Three possible outcomes are envisaged: if the EMU opts for maintaining the “Maastricht Agreement” and continues towards rule-based fiscal integration to preserve formal national sovereignty, the intergovernmental nature of the EU will be irrevocably fixed at the expense of democratic decision making; the democratic loss could be, to some extent, balanced by a perfectly smooth performance, which however is unlikely (Chapter 5 discusses the limits of output legitimacy in detail). While the formal competences of parliaments will be maintained to fulfill constitutional requirements, the freedom of action of national authorities would have to be restricted as much as possible through a rule-based framework, and the residual decision-making powers on fiscal and economic policy would have to be delegated to an intergovernmental institution, such as an enhanced version of the Eurogroup. Under this option, output legitimacy (Scharpf, 1970; 2009) would continue to be the driving legitimization factor for the EU, although it is not clear whether output legitimacy is efficient when applied without an ex-ante convergence of

---

<sup>7</sup> The identity argument, known as “No demos thesis”, was popularized by the German Federal Constitutional Court in 1993. The argument is widely discussed in Nicoli (2015), as well as in chapters 2 and 5 of this dissertation, along with the other vertexes of the pseudo-trilemma and its relationship the well-known Rodrik (2007) trilemma and its application to the Eurocrisis by Crum (2013).

economic fundamentals. Without ex-ante economic convergence, any constitutionalized fiscal treaty risks of setting not only “the rules of the game”, but also its winners (See chapter 5, or Nicoli 2015). The logic of the third trilemma will be discussed in detail in chapter 5, after having reconstructed with precision the theoretical logic leading to each of the vertexes of the trilemma. The next chapter addresses instead the fundamental question of the functional nature of the Eurocrisis, exploring whether pre-crisis divergence and lack of appropriate European institutions have contributed to the Eurocrisis, thus finding evidence if favour of the macro-functional explanation of the crisis outlined here.

If, on the other hand, the EU were to opt for fiscal integration and democratic decision making, an overhaul of the competences of the European Parliament (and of its composition) would be needed. It is unclear, however, whether empowering the European Parliament to enact fiscal and economic policy would be possible without some degree of common identity. Many established nation-states in which national identity is absent or in tatters struggle to enact redistributive fiscal policies and are subject to constant break-up tensions; without a strong(er) European identity, the newborn European Federation would likely suffer from the very same disease. Yet, the instruments the EU currently has in place provide few means for stimulating the growth of a common sense of belonging among Europeans.

The last solution – the demise of the EMU – is by no means easier than the previous options. Not only would it require an enormous political effort to deal with short term costs, but it also would unleash a dynamic of dis-integration that would be difficult to reverse. As shown in the previous sections, the EMU was not born out of the political will of an elite of federalist thinkers; rather, it was a solution in the making for almost three decades following the original Werner report in 1971. Removing the Single Currency would require the return of either high monetary instability in the continent or of capital controls. Either way, the Single Market would be in danger: since it would risk collapsing under “beggar-thy-neighbour” monetary policies in the former case, or be strongly reduced by limited international transactions in the latter. No doubt that without monetary integration and with a strongly reduced single market, the foundations of the European post-war order would be dramatically shaken. Not differently from previous “critical junctures” (Fabbrini 2015), the solution to this specific crisis will require a long process of deliberation and would involve, eventually, a comprehensive package of deals in order to grant a treaty

change suitable for all member-states. Similarly, with the Single European Act and the Treaty of Maastricht, additional fundamental issues would have to be included in the conclusive deal, addressing not only the legitimacy question at stake in the pseudo-trilemma, but a multiplicity of needs and expectations on European integration from a plurality of member-states. Yet the rise of popular discontent, coupled with the simultaneous pressure from multiple crises –the Eurocrisis, the migration crisis, the Russian pressure on the eastern border, and the British quest for increasing non-EMU countries’ autonomy from the Institutions – may create the momentum necessary to initiate the process of Treaty revision.



## Chapter Three: Is the Eurocrisis a Functional Crisis? A quantitative investigation of the Eurocrisis' endogeneity.

### Abstract

Since 2008, the European Union and the Euro Area in particular have substantially strengthened their integration in the matter of macroeconomic, fiscal and financial cooperation. The harsh necessity of finding a solution to the never-ending Eurocrisis has constituted, of course, the main engine of this wave of integration, which —still short of achieving full fiscal integration in the Eurozone— has nonetheless generated a shift of competences from the member states to the Union that was unthinkable fifteen years ago. Yet Functionalism, the main theory of crisis-led integration, has been largely neglected by contemporary scholarship on the Eurocrisis. While the uttermost implications of the Eurocrisis for integration and democracy begin to unfold in elections across the continent, the goal of this paper is to put the central hypothesis of contemporary Functionalism at test. Methodologically, after constructing an Index of Crisis Intensity (ICI) with the aim of capturing both the financial and social dimension of the crisis, the paper explores quantitatively through a series of comparative regressions whether the different intensity in the ICI is completely, partially or not connected at all with the Eurozone membership and with the effects it entailed in the first 10 years of EMU.





# Is the Eurocrisis a Functional Crisis? A quantitative investigation of the Eurocrisis' endogeneity.

## 1. Introduction: Functional integration theory in times of crisis

Since 2008, the European Union and the Euro Area in particular have substantially strengthened their integration in the matter of macroeconomic, fiscal and financial cooperation. The harsh necessity of finding a solution to the never-ending Eurocrisis has constituted the main engine of this wave of integration, which —still short of achieving full fiscal integration in the Eurozone— has nonetheless generated a shift of competences from the member states to the Union that was unthinkable fifteen years ago. Yet Functionalism, the main theory of crisis-led integration, has been largely neglected by contemporary scholarship on the Eurocrisis. The goal of this paper is to put the central hypothesis of contemporary Functionalism at test, in the attempt of recovering some of the valuable insights this century-old theory may still yield. Functionalism, as a theory, has undergone several cycles of rethinking: from the original approach proposed by Mitrany in 1917 (Mitrany, 1975) to the Neo-Functionalism of Haas (1958; 1964, which I will call hereafter *microfunctionalism*) to the Neo-Neo Functionalism of Schmitter (2002; 2008, which will be referred as *macrofunctionalism* in this paper) and Postfunctionalism of Hooghe and Marks (2009).

All versions of Functionalism share two fundamental elements: path-dependency and “spilling effects”. This is particularly evident in Schmitter’s “macrofunctionalist” approach, that attempts to explain supranational integration as a series of cycles of crisis-led integration; remarkably in line in fact, with policy-makers’ understanding of functional integration:

While in the original versions the “spilling mechanism” was understood as a set of unintended consequences of integrating one particular set of policies (Haas, 1964) and thus had a clear forward-looking dimension known as spillover, newer versions of the theory took into account a larger set of possible reactions to a crisis: spillback (i.e. removal of the critical element of integration which generated the crisis in the first place); spill-around (transferring of competences in an intergovernmental setting). In other words, functionalism expects that a reaction to an endogenous crisis is qualified over the decisions taken on two dimensional axes: increase (decrease) in the range of integrated policies, and increase (decrease) of supranational vs. inter-governmental decision making. Moreover, macrofunctionalism puts particular emphasis on crisis-led functional integration. Functional integration is, by definition, partial and incomplete: it concerns the most limited amount of functions, powers and institutions needed to address a particular concern. This may lead to certain advantages, but may entail “unforeseen consequences” by creating new problems which did not exist when functions and competences were held at the same level (Haas, 1964). The functional integration dynamics is thus characterized by a “crisis>integration>crisis” continuous dynamics.

More specifically, Macrofunctionalism defines as a *functional crisis* a crisis characterized by (a) *endogenous determinants* and (b) “*spilling-like*” *resolution*, either in term of further integration, or beginning of disintegration. The definition of *endogenous determinants* must be carefully calibrated: it does not imply, in fact, that the crisis originated within the countries involved in the integration process (although it might well be the case) but that their response is hindered, or made counterproductive, by their current degree of integration. In fact, while there is little doubt that the creation of the EMU responded to specific economic problems through sectorial integration (see Chapter 3), whether creating a single currency without political institutions is appropriate is an element of economic debate since Balassa (1961), Mundell

(1960; 1961) and Kenen (1969). The goal of this paper is thus to assess whether the Eurocrisis can be understood as a functional crisis, looking in particular to (a), the endogenous nature of the crisis.<sup>1</sup>

Finding an answer to (a), however, requires a dive into theoretical and empirical macroeconomics. As a matter of fact, this is no new field: an abundant amount of literature has been produced on the issue of the origins of the Eurocrisis. At this regard, section 2 reconstructs the scholarly debate on the origins of the Eurocrisis. Most of the literature, however, aims to determine whether particular policies (in particular, fiscal policies) have ignited the crisis, but fails to answer the question we are interested in, i.e. whether the Eurocrisis can be defined, broadly speaking, as *endogenous*. Section 3 provides an answer based on political economy and descriptive statistics; section 4 discusses the econometric model: at this regard, I start by building a new indicator of the crisis itself, aiming to find out its determinants through panel analysis, whose results are presented in section 5. The conclusions discuss the results from the perspective of Functional Integration Theory.

## **2. A clash of narratives: what caused the Eurocrisis?**

Why Europe is in crisis? The dominating narrative has mutated a few times between 2008 and 2014: “financial crisis” before 2010, “debt crisis” thereafter until early 2011; Eurocrisis since then, adding an emphasis on the systemic nature of the crisis and on the crossborder economic asymmetries. This semantic evolution captures the fluid understanding scholars and policy makers have of the crisis and of its relation with the global financial crisis of 2008. The debate over the responsibilities of the EMU in the Eurocrisis is, despite of the very large number of contributions (or maybe because of it) still a very lively and open to new insights. Literature can be broadly articulated in two separate research strands: whether the design of the Monetary Union is the “original sin” of Europe, and thus the ultimate cause of the crisis; and whether the lack of appropriate institutions prevented the Eurozone to safely recover from the global financial crisis,

---

<sup>1</sup> We are particularly interested in hypothesis *a* not because we disregard the importance of investigating the quality of the response to the Eurocrisis, but because it is evident that the crisis has brought limited new integration. What Functionalism currently lacks is a coherent theory enabling a prediction of why, given certain conditions, the response to a functional crisis is qualified as a spillover, spillback or spillover. In other words, how the degree of integration evidently produced by the Eurocrisis is qualified from a functional perspective, and for what reasons it has taken the form of –let’s say– spillover instead of spillback, constitutes an interesting question from the point of view of recovering functionalist theory but falls outside of the narrow goal of this paper, which aims to assess whether we are observing a functional dynamics currently unfolding.

thus being the cause of the Eurocrisis' intensity and persistence. While early studies emphasized the contagion dynamics between the global crisis and the European debt crisis, a second wave of research tried to identify the specificities of the European crisis, especially in light of the sustained recovery experienced by non-EMU countries, US and UK in particular.

### *2.1. Crisis prevention: EMU as original sin?*

Since Krugman's (1991; 1993; Krugman & Venables, 1996) "agglomeration" thesis, scholars have discussed whether a Monetary Union increases or decreases divergence among participating countries. Early work on the countries participating in the Single Currency (De Grauwe, 1998; Bayoumi & Eichengreen, 1996A, 1996B, 1998) suggested that countries participating in the EMU were not enough converging but rather split into core and peripheral countries. Thus, a first set of explanations of the Eurocrisis relies on pre-crisis divergence among Eurozone members. "Divergence" arguments may further be split into two approaches, depending on whether they stress debt and deficit performance (1) or macroeconomic and labour policies (2). Institutions like the ECB and the IMF, while involved in the crisis resolution in Greece, have initially emphasized the country's failure in fulfilling Stability and Growth Pact (SGP) fiscal obligations as a cause of the crisis. Moreover, the over-spending policies of certain countries before the crisis undermined their counter-cyclical capacity during the global recession in 2008. This was due, in part, to the shortcomings of the SGP, which failed to provide the correct incentives for fiscal policy (Benétrix & Lane, 2013). Other scholars, however, point out that several countries did not run excessive deficits or debt: it's the case, for example, of Spain and Ireland (Krugman, 2012). Rather, they were experiencing macroeconomic and financial imbalances amplified by a weak banking supervision and no joint banking union.

Building on an existing body of literature on disequilibria, divergence and adjustment among EMU members (Mongelli & Vega, 2006; Angeloni & Ehrmann, 2007), those authors point at the divergent labour costs, competitiveness profiles and related capital flows as a leading cause of the crisis (Holinski et al 2010; Gros, 2012; Knedlik & Schweinitz, 2012). Similarly, others point to the explosion of domestic lending and construction sectors, which drove inflows of capitals in non-productive sectors fuelling inflation and deteriorating the current account (De Grauwe, 1998; Adam et al., 2012), setting the scene for a within-

EMU sudden stop when the link between banking and sovereign sectors became exposed (Merler & Pisani-Ferry 2012A). Moreover, De Grauwe and Ji (2012) observe that the crisis may be attributed to the effects of financial markets' mistakes in pricing risk: while an underestimation of risks has induced financial markets to over-lending policies to governments and households before the crisis –leading to higher inflation, excessive spending, rising labour costs and decreased competitiveness— under-lending (and thus spikes in interest rates) are causing excessive austerity, which in turn weakens the Banking sector further in a classical banking-sovereign “vicious circle”; further amplified in debtor countries as divergent labour costs and the loss of competitiveness also have implications for the expected fiscal policy of the concerned country. Finally, Stiglitz (2016a, 2016b) argues that “the Euro was flawed at birth” as fiscal constraints and restrictive monetary policies would have irremediably generated a crisis (Stiglitz, 2016b)<sup>2</sup>

While in disagreement on the key elements of pre-2008 divergence that are ultimately linked to the Eurocrisis, scholars in this strand tend to believe that Eurozone design was in part responsible for the Eurocrisis because it failed to foster convergence producing distortive incentives for diverging fiscal and labour policies, which –coupled with irresponsible and unsupervised banking sector—set the stage for later disintegration. The EMU failure is thus a failure of effective coordination and incentives. Against this view, it has been claimed that national factors played an essential role in divergence: Greek's decision of falsifying fiscal reporting was not a failure of coordination; the capital inflow leading to housing bubbles in Spain, Portugal and Ireland, although fostered by crossborder banking and the Single Currency, was not caused by wrong policy coordination; it was a national decision of certain governments (and not others) in certain countries to ignore the SGP regulations and misuse the “Euro-dividend” on interest rates;<sup>3</sup> moreover, as the supervision and regulation of the banking sector was, in most part, a national competence until the establishment of the European Banking Authority in 2010, national regulators were responsible for the excesses of their domestic banking sector as well.<sup>4</sup> Therefore, from this point of view, the Eurocrisis was a failure of national economic policy-making rather than a failure of coordination and governance

---

<sup>2</sup> Op-Ed on the Financial Times <http://www.ft.com/cms/s/0/dbbd151c-62f4-11e6-8310-ecf0bddad227.html>

<sup>3</sup> Some even claim there has not been any “Eurodividend” on interest rates at all, because the fall in interest rates after 2000 is rather a global phenomenon than a purely European one.

<sup>4</sup> Although one shall acknowledge that, in the pre-2010 world, where national banking supervision was severed along national borders, national regulators had little capacity of assessing the situation of large cross-national banks.

mechanisms at EU level. Finally, Sinn and Wollmershäuser (2011; 2012) consider that macroeconomic imbalances, even if partially grounded in labour cost differentials, have been fuelled by loose monetary policy and hidden bail-out policies enacted by the ECB which have generated an unsustainable growth of consumption in weak member states; the crisis is not due, in their view, to a particular institutional design, but rather to the kind of policies enacted by the ECB before and during the crisis.

## *2.2. Crisis management: Eurozone Design Failures?*

The debate on the responsibilities of the Eurozone design *during* the global and European crises is even more articulated. Two main strands can be identified. On the one hand, the “Keynesian textbook” understanding of the crisis has been promoted by scholars like Stiglitz (2015, 2016b)<sup>5</sup> according to which the crisis is fundamentally caused by the Euro as a fixed exchange rate system without common fiscal policy. On the other hand, the “Mainstream textbook” narrative, which proposes a more nuanced view anchored in a large number of factors. The “Mainstream textbook” narrative, generally, goes as follows: an exogenous shock (the global financial crisis) impacts on the EU; the effects are symmetric across the continent but the response, and its sustainability over time, is asymmetric and varying according with the strengths and weaknesses of each country, because there is no fiscal integration and thus countries have to act on their own finances only. Divergence ensues and the lack of exchange rates prevents smooth adjustment afterwards. The core issues are therefore three: (i) the connection between the global crisis and the Eurocrisis, (iii) the emergence of asymmetry, (iii) and the management of the adjustment path towards the new equilibrium.

Enders et al. (2013) claim that, although the introduction of the EMU has actually reduced asymmetry, the particular institutional setting had generated a heterogeneous response to the global crisis, thus fostering asymmetry after 2009; Beirne and Fratzscher (2013) show that a “wake-up-call” type of contagion happened between 2009 and 2011, when financial markets became unexpectedly sensitive to fiscal fundamentals’ differences which emerged during the quiet EMU years 2001-2007 and were inflated by policies enacted in reaction to the 2008 crash, but which were largely ignored by financial markets before

---

<sup>5</sup> Interview with Internationale Politik Gesellschaft.

<https://www.youtube.com/watch?v=H9EdGYyLcO0&feature=youtu.be>

the crisis' outbreak. This reasoning mirrors the position of the European Commission (2013), for which the large deficits run by countries as a response to the global crisis matched with a banking sector under heavy stress, implying both (a) a wave of public rescues (which further increased debt) and (b) a spike in interest rates (as banks started to sell shaky holdings on public bonds). In this narrative, the role of EMU design appears of secondary importance.

It has been argued, however, that the lack of a Banking Union increased the stress on both the governments and the banking sector, because it provoked public rescues ultimately fuelling the banking-governments loop. Similarly, the lack of a sovereign Central Bank as a lender of last resort left the countries unable to provide the necessary liquidity to bail out banks, moving the entire burden on the governments, equally lacking a lender of last resort; De Grauwe and Ji (2013a) show in fact that the Euro Area crisis had some self-fulfilling features precisely because of the hampered capacity of the ECB to grant public bonds' liquidity; this was known by financial actors which staged a run. At this regard, Merler and Pisani-Ferry (2012a) identify clear episodes of "sudden stops" in weak EMU countries, followed by expansion of public lending as a compensation of massive outflows of private capitals. On the other hand, sudden stops may be also linked to macroeconomic imbalances: the extended deterioration of competitiveness positions of weak EMU countries before and during the Eurocrisis has brought about a vibrant debate on the consequences of such imbalances for the stability of the Eurozone. One of the implications of divergent competitiveness is a deteriorating foreign assets' position for weak countries, which may lead to capital outflows and worsening of the TARGET 2 accounts of the involved countries, which may constitute a threat for the creditor countries were the debtor countries obliged to leave the Eurosystem. Therefore, De Grauwe (2012) suggests the Eurozone to implement a "symmetric adjustment policy" where core countries contribute as much to the adjustment process as peripheral countries. The role of the German strategy, based on wage moderation and export-led growth has been widely discussed as a potential source of asymmetry (Bonatti & Fracasso, 2013), leading some to conclude that German wage moderation contributed to the crisis as much as peripheral countries' inflation (Bofinger, 2015) and could have been an explicit attempt to enact a "beggar-thy-neighbour" growth strategy (Wren-Levis, 2015). Again, while this effect may be interpreted as a purely domestic phenomenon, it has been pointed out that a stronger coordination of labour policies might have



prevented this outcome, as the EMU coordination mechanism (the Open Method of Coordination, OMT) failed to deliver effective results (Ioannou & Sacca, 2011).

A second element of debate is the role of monetary and fiscal policy during the crisis. Sinn and Wollmershäuser (2012) believe that accommodating ECB policies until 2010 and since 2011 are a leading cause of the persistence of the crisis because it decreased pressure on peripheral governments to adjust their balance-sheets, delaying the needed fiscal and macroeconomic adjustment. Against this view, it has been argued that the early rise in interest rates, enacted in 2010 by the ECB and in contrast with the policies of both US and UK central banks, has been one of the leading causes of the re-igniting of the crisis and of its regionalization within the Monetary Union; the interest rate rises in April and July 2010 worsened the credit conditions of peripheral member states raising doubts on the solvability of their governments, thus being one of the causes of the sudden stops. As a consequence, confidence in the stability of the recovery collapsed, plunging the continent into a double-dip recession. In this view the real aspect differentiating the Eurozone from the US and UK is the different fiscal and monetary policy implemented (although being locked into a monetary union does indeed constitute part of the puzzle). Building on a revised paper of Perotti (2011) on the effectiveness of austerity policies during a crisis and on the literature on fiscal multiplier and front-versus-back-loaded fiscal consolidation, several authors have claimed that, at best, austerity policies during a financial crisis are self-defeating (Holland & Portes, 2012), not least because they might have been not truly needed in the Eurozone (DeLong & Summers, 2012). The absence of a “lender of last resort” enabled to provide support for both public finances and lending institutions created an “instability circle” between distressed sovereigns and their national banks (Acharya et al, 2011; Obstfeld, 2013). This, in turn, pointed to the absence of a lender of last resort and of a Euro Area Banking Union as the key missing features of the EMU (Merler & Pisani-Ferry, 2012b; Pisani-Ferry, et al., 2012; Howarth & Quaglia, 2013; Gros & Schoenmaker, 2014). Moreover, De Grauwe and Ji (2013a) argue that the dynamics of the Eurocrisis can be presented as a story of self-fulfilling crisis where the lack of commitment of the central bank creates uncertainty over the sustainability of public deficits, thus generating additional effort from governments attempting to show to financial markets that they are facing an illiquidity crisis and not an insolvency one; but the additional austerity achieved in this way pushes the economy further downwards, undermining debt sustainability even further and thus transforming illiquidity into insolvency. De Grauwe

and Ji (2013c) provide additional evidence pointing at “panic-driven austerity” as a leading cause for the worsening of the Eurocrisis, having in part caused the capital outflow from peripheral countries. Similarly, the self-defeating nature of austerity is depicted by Tamborini (2014) who claims that not only austerity has provoked higher unemployment rates, but has hampered financial stability of the concerned countries.

Finally, a few authors have claimed, in various phases, that the Euro was so badly conceived, producing divergence and lacking common adjustment mechanisms, that Europe (or at least some countries) would be better-off by dismantling it (Roubini, 2011, 2012; Arghyrou & Tsoukalas, 2010, 2011; European Solidarity Manifesto, 2013; Melitz, 2014; Kawalec & Pytlarczyk, 2015). Although this paper won’t discuss their theses in detail, it is clear that they attribute to the simple existence of the Euro Area many of its economic problems.

### **3. Comparing contrasting views: alternative explanations in descriptive statistics**

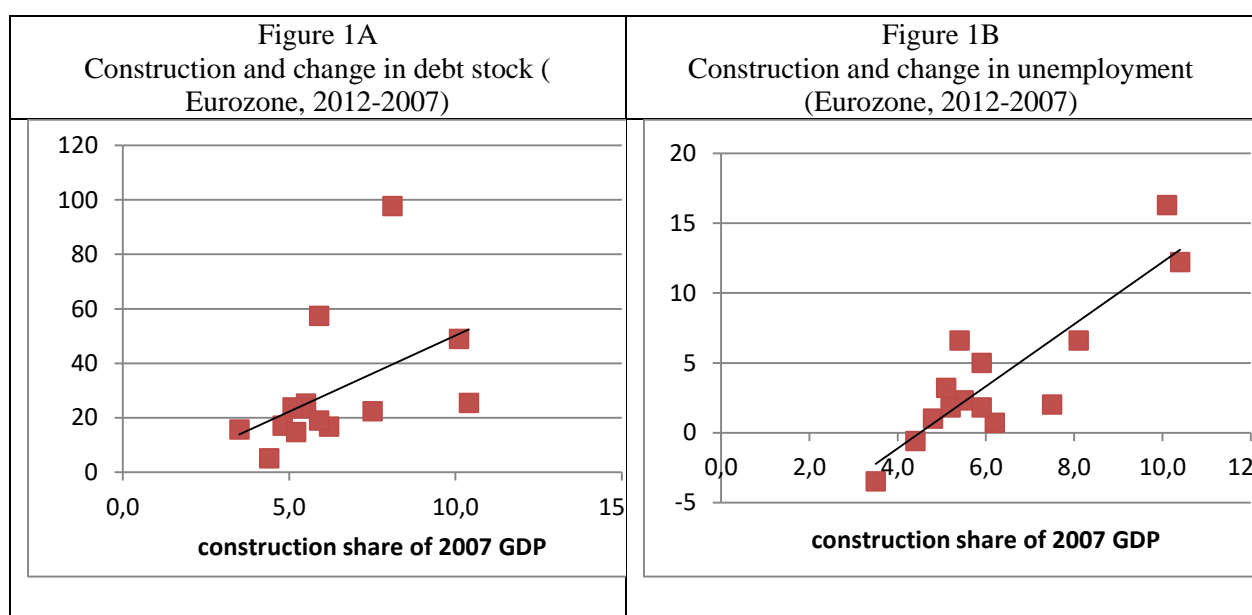
As shown in the previous section, scholars generally fail to agree on the responsibilities of the Euro and of the Eurozone governance institutions as origins of the crisis and reason for its endurance. Several distinct positions have been highlighted in the previous section. It must be noted that contrasting views often start from the same dataset attributing its dynamics to different elements: this is the case, for instance, of the labour costs’ dynamics. Before moving ahead with the econometric model, this section provides an overview of the different claims as they are anchored in descriptive statistics.

#### *3.1. A combination of national diseases*

The first thesis on the Eurocrisis postulates that the Euro does not suffer from an “original sin”; the causes of the Eurocrisis are rather to be found in country-specific issues (housing bubbles in Spain and Ireland; public debt in Greece; structural public spending in Italy; banking sector weaknesses in Cyprus) which led to both fiscal and macroeconomic imbalances. On the macroeconomic side, this points to debt accumulation, competitiveness and housing market bubbles as critical factors.

Debt, in particular, has been perceived as the main cause of the Greek crisis since the trust in the deficit figures reported by the Greek government collapsed in 2010, following the well-known Eurostat scandal. In 2011, the Greek debt reached already 170% of the country’s GDP. Greece, along with Italy and Belgium,

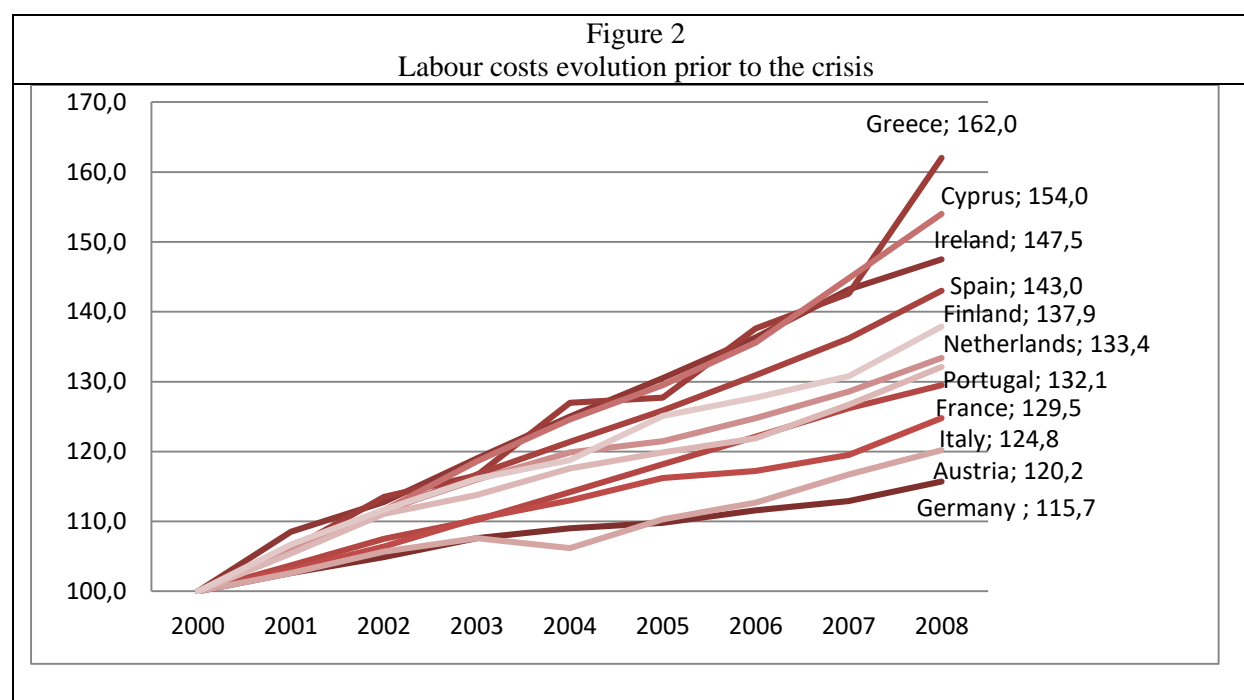
constituted one of the three countries far-off from the 60% debt/GDP criterion for Euro adoption; other crisis countries, like Spain and Ireland, not only met (or where very close to) the 60% threshold at the moment of accession, but managed to reduce it substantially before the crisis; Spain achieved a 42% reduction of its 1999 public debt stock in the period 1999-2007, Ireland of 51%; Cyprus experienced a total public debt growth of 2% of GDP on the whole period. Of the programme countries, only Portugal (along with Greece) experienced a substantial growth of the debt stock, from 51% of GDP in 1999 to 68% in 2007.



For all these countries, the overshooting of public debt occurred in the first two years of the crisis, as a consequence of the expansionary fiscal policies enacted, of the collapse of GDP, and of the nationalization of the troubled banking system. Pre-crisis over-accumulation of public debt appears thus to be a potential cause of the crisis only for Greece and, in a lesser measure, for Italy, which also failed to reduce its 1999 stock of debt substantially in the first 8 years of EMU.

However, public debt is only a factor among many. Other national factors however may play a role, such as private debt. In particular, the size of the construction sector has been considered an important driver of the crisis, provided that the original “subprime crisis” imported from the United States was the main source of banking weakness and drove nationalization of assets in Ireland and Portugal. At this regard, figure 1A shows the correlation between share of GDP in the construction sector in 2007, and change in public debt stock between 2008 and 2012 for all Eurozone countries. The correlation is moderately positive (0.47) as

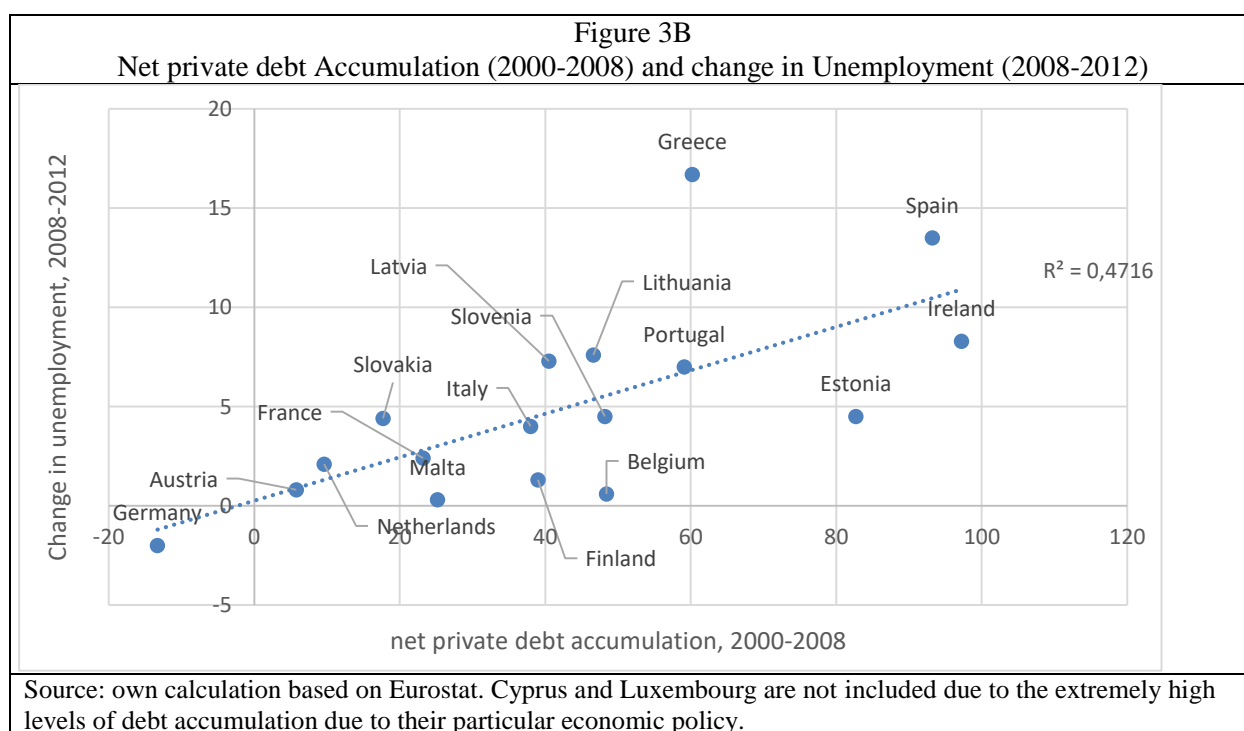
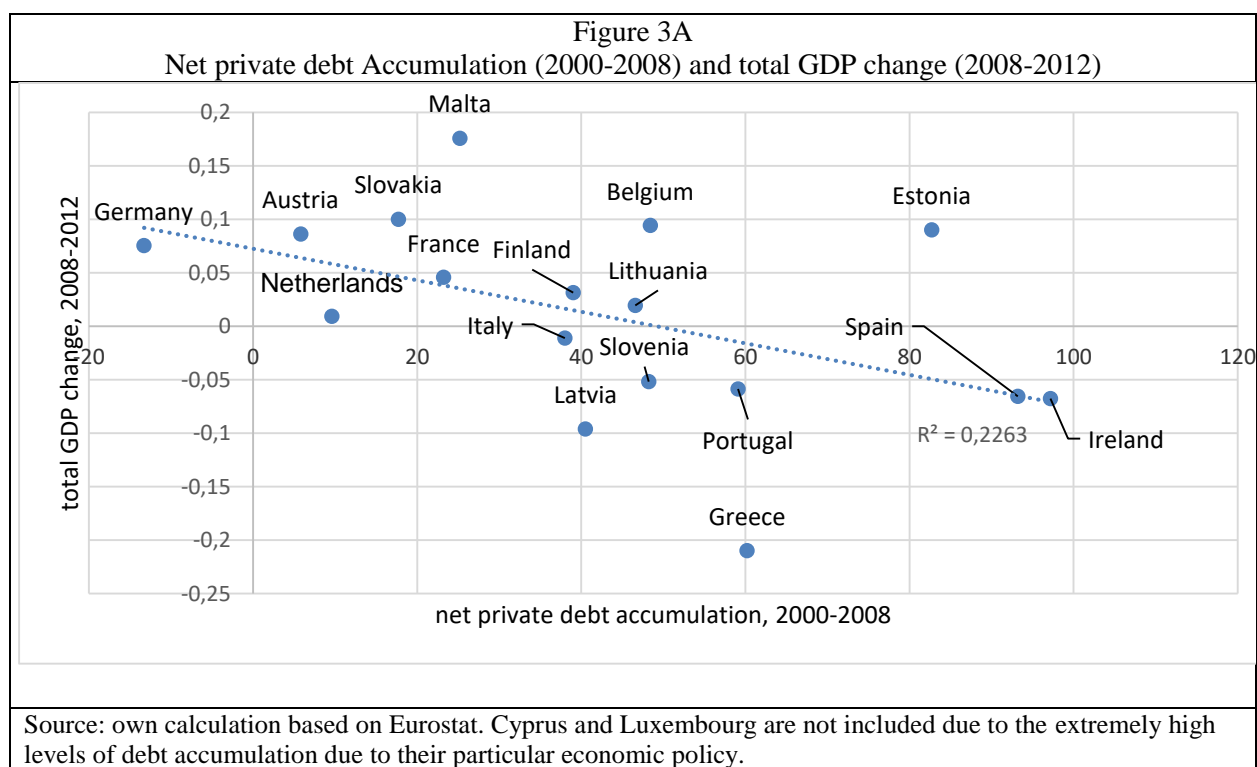
expected given the housing bubble experienced by several countries; in the EU as a whole, however, the correlation is weaker (0.31). The correlation between change in unemployment in the crisis period and the pre-crisis share of the construction sector is even stronger (figure 1B): in the EU as a whole it stands at 0.66, while in the Euro Area reaches a staggering 0.88.



Finally, labour costs evolution is often cited as a typically national cause of the crisis (Lebrun & Perez, 2011). As the narrative goes, peripheral countries have enjoyed higher credit, higher consumption and higher wages during the “good” EMU years, worsening their competitiveness in the international markets. The well-known Figure 2 shows the evolution of nominal relative labour costs for selected EMU countries. Four of the five Euro Area countries receiving financial assistance after 2011 score the highest (relative) increases in labour costs over the period 2000-2007. However, the correlation between increase in labour costs in the period 2000-2007 and the change in unemployment 2008-2012 is 0.31, rather limited if compared with the 0.88 correlation in figure 1B.

As such, moreover, a change in relative labour costs may also indicate that the countries are simply converging from an initial divergent point, and thus is to be regarded as a natural phenomenon in currency unions (as well as the associated external deficit; Balassa, 1961). A variant of this point of view states that The Eurozone holds an indirect responsibility for the Eurocrisis because its design lacked appropriate

governance, failing to achieve coordination, providing wrong incentives, and provoking divergence both on fiscal performance and on competitiveness.



According to this reading the crisis was exogenous and symmetric in the very early days, but -by hitting countries with asymmetric structures- produced asymmetric outcomes, which could not be prevented given the lack of coordination and integration (Enders et al, 2013, Beirne & Fratzscher 2013; Sinn, 2014).

A third element arrow in the “domestic” explanation of the crisis relies on pre-crisis debt dynamics. Although the “public debt” narrative was dominant in the public debate in 2010 and 2011, the persistent stress experienced by the banking sector, as well as the fact that several Euro Area states most hit by the crisis (such as Spain and Ireland) did not accumulate large public debt until the crisis, moved the discussion to private debt stock. Indeed, some relation appears to exist: figures 3A and B present the correlation, within the Euro Area, between total private debt accumulation in the years before the crisis (2000-2008) and both total growth (3A) and total unemployment (3B) in the period 2008-2012.

In both cases, a strong (negative) connection appears between pre-crisis debt accumulation and post-crisis growth, as well as an even stronger (positive) connection between pre-crisis debt accumulation and crisis-related unemployment. It could be argued, however, that the very existence of the Monetary Union, fostering inter-national lending between the participatory countries and fostering intra-Euro trade ties, would lead to a substantial increase in private debt (De Grauwe, 1998; Merler & Pisani-Ferry, 2012A).

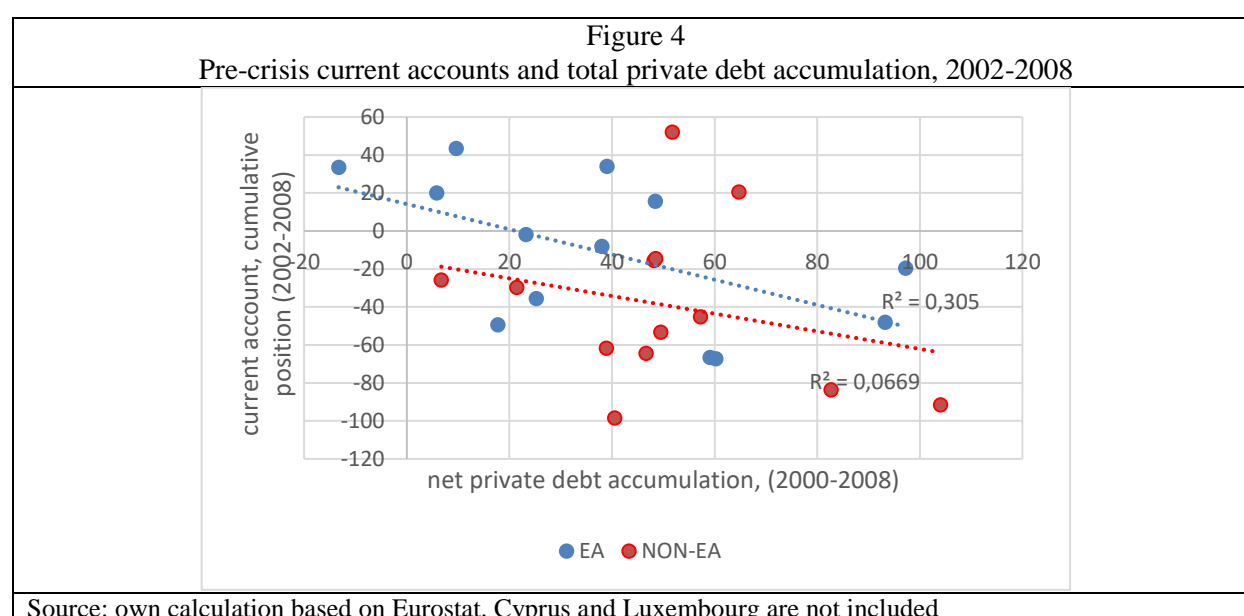


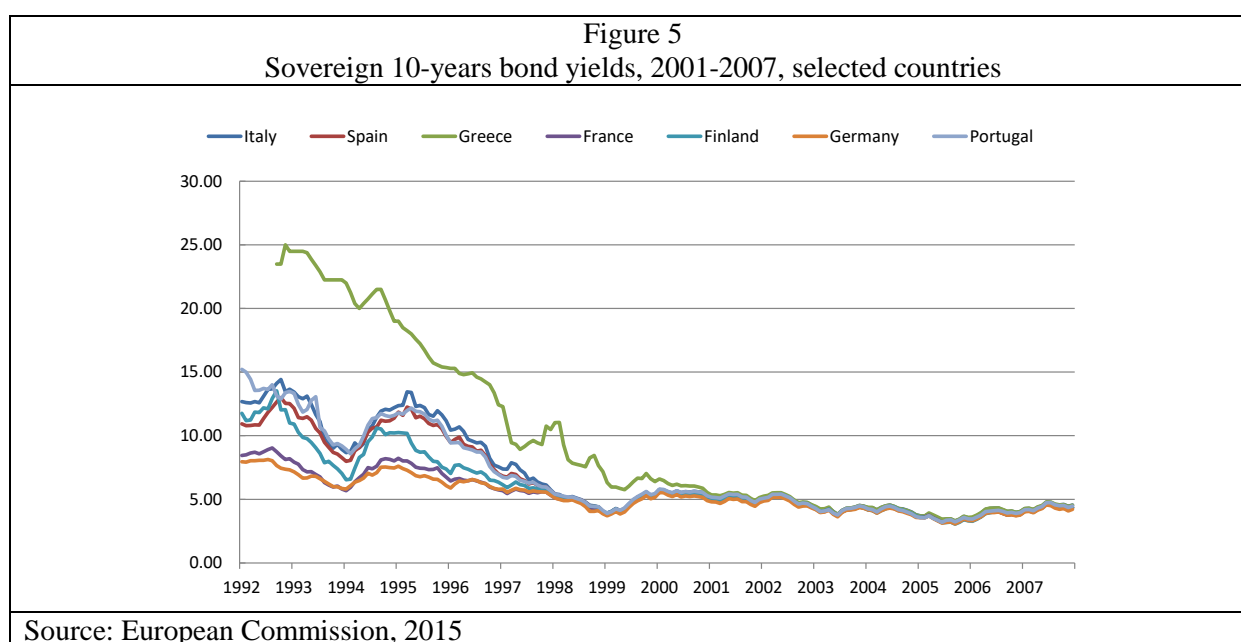
Figure 4 shows the correlation between cumulative current account positions in the years (2002-2008), and the equivalent private debt accumulation, divided for Eurozone and non-Eurozone members. The correlation and the  $R^2$  are fairly higher for the Eurozone (Correlation 0.55 versus 0.25;  $R^2$  0.3 versus 0.07), suggesting that indeed participation in the Eurozone may have contributed to inflate domestic debt through cross-border trade and lending. It may also indicate, however, that Euro Area countries, which tended to be the more advanced and the wealthiest in the whole EU (with the exception, perhaps, of the United Kingdom) tended also to be more financially integrated than non-Euro counterparts. The trend in both groups is comparable, provided different in magnitudes that may be attributed to the cited effects.

### *3.2. A wrong policy mix at national and European level.*

The second thesis on the Eurocrisis postulates that a wrong fiscal and policy mix was enacted both at national and European level. Thus, the Euro (as a currency) bears no direct responsibility in the crisis, but the particular fiscal and monetary policies enacted during the crisis have worsened, instead of eased, the economic downturn and/or adjustment. The responsibility is shared by fiscal and monetary policy-makers at European and National level (Sinn & Wollmershäuser, 2012; Holland & Portes, 2012; in a lesser extent, De Grauwe & Ji, 2013c). This working logic of the argument is shared both by scholars blaming austerity, and scholars blaming too little austerity and too accommodative monetary policy. In general, this line of reasoning points to ECB rates evolution and to fiscal stance during the crisis, either blaming too much austerity or too little consolidation effort in member states.

The debate has been marked by heated contributions concerning both fiscal and monetary policy stance. Concerning the latter, two leading theses have emerged: the “moral hazard” thesis and the (lack of) a lender of last resort. According with the moral hazard thesis, it is essential that markets are enabled to correctly price the risk differentials between countries in order to maintain an appropriate market pressure on governmental decisions on fiscal policy. Failure in correct pricing of the risk will result in governments with less sustainable fiscal policies to receive an incentive to continue with their expansionary policies instead of reducing their debts. In fact, the interest rate convergence experienced by peripheral member states in the period 2002-2007 (figure 5) removed any market incentive to fiscal discipline. Therefore, if accommodating monetary policy is deemed to delay adjustment, decisions such as the decrease in interest

rates in late 2011, and –even more- the “whatever it takes” famous talk from the ECB President Mr. Draghi in June 2012, followed by the Outright Monetary Transactions Programme (OMT) in October 2012 and the Quantitative Easing since January 2015 have reduced the incentive for governments to adjust their balance sheets, weakening the fiscal targets commitments that member states signed in the Treaty on Stability, Coordination and Governance (known as “fiscal compact”).

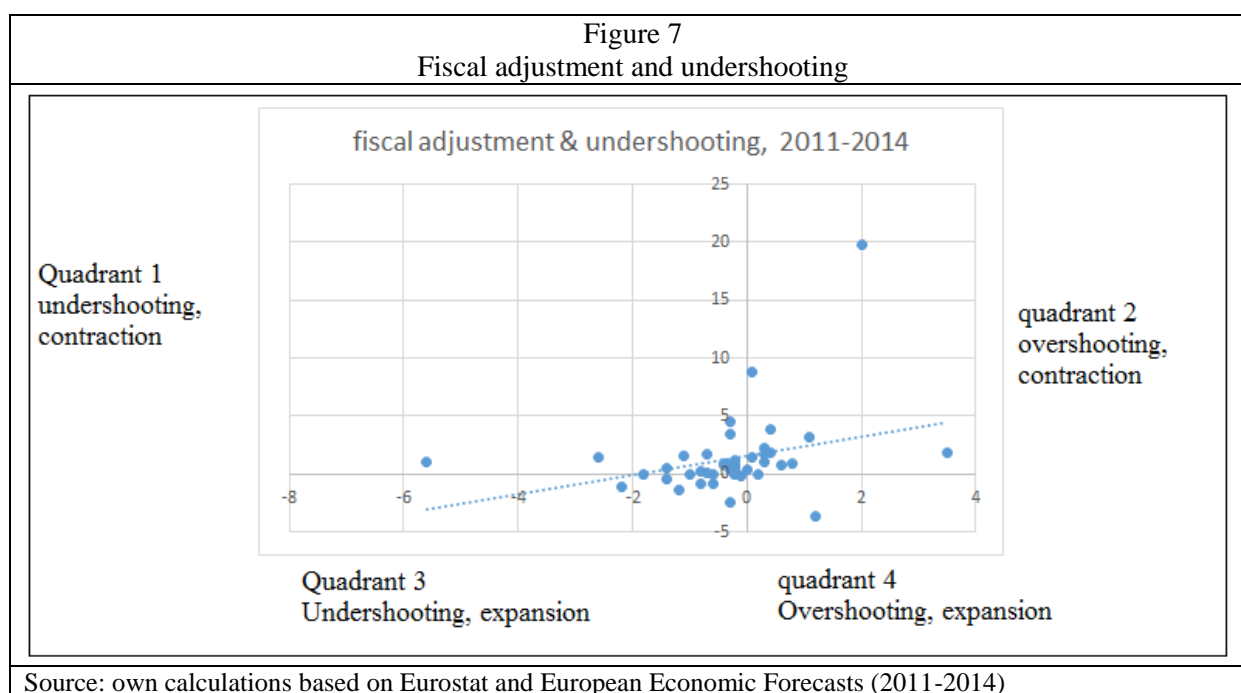
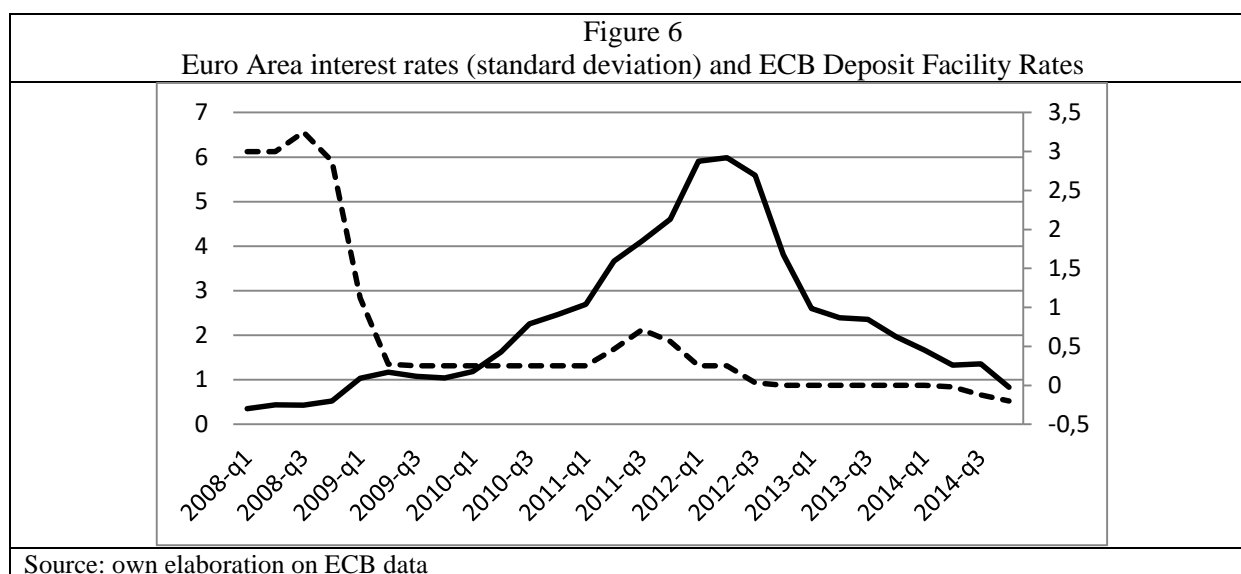


Against this stands the opposite vision: monetary policy was in fact too restrictive, the rise in interest rates in 2011, accompanied by austerity policies, happened too early, causing an outflow of capitals from the peripheral countries with heavy consequences for their financial stability. Figure 6 shows the evolution of the standard deviation of the Euro Area 10-years yields, which measures divergence in risk of public bonds (continuous line). It clearly begins to increase in early 2010, accelerates up to a 30% quarterly growth rate in Q2-2011 and begins to decline at the end of Q2, 2012 coincidentally with Draghi’s speech which was perceived as the ECB stepping in as a lender of last resort. Figure 6 also shows the evolution of the Key Interest Rate of the ECB (quarter on quarter, dotted line).

Although the correlation of the two indicators is rather weak (0.39 in the 2009-2014 period), some elements suggest a connection between the variables: for instance, the Q2-2011 increase in interest rates corresponds with the maximum acceleration of the SD’s growth rate. This would imply, according with the proponents



of the argument, that the ECB's rising rates have accelerated the capital outflows from peripheral countries, increasing the pressure on governments to implement ill-fated austerity policies.



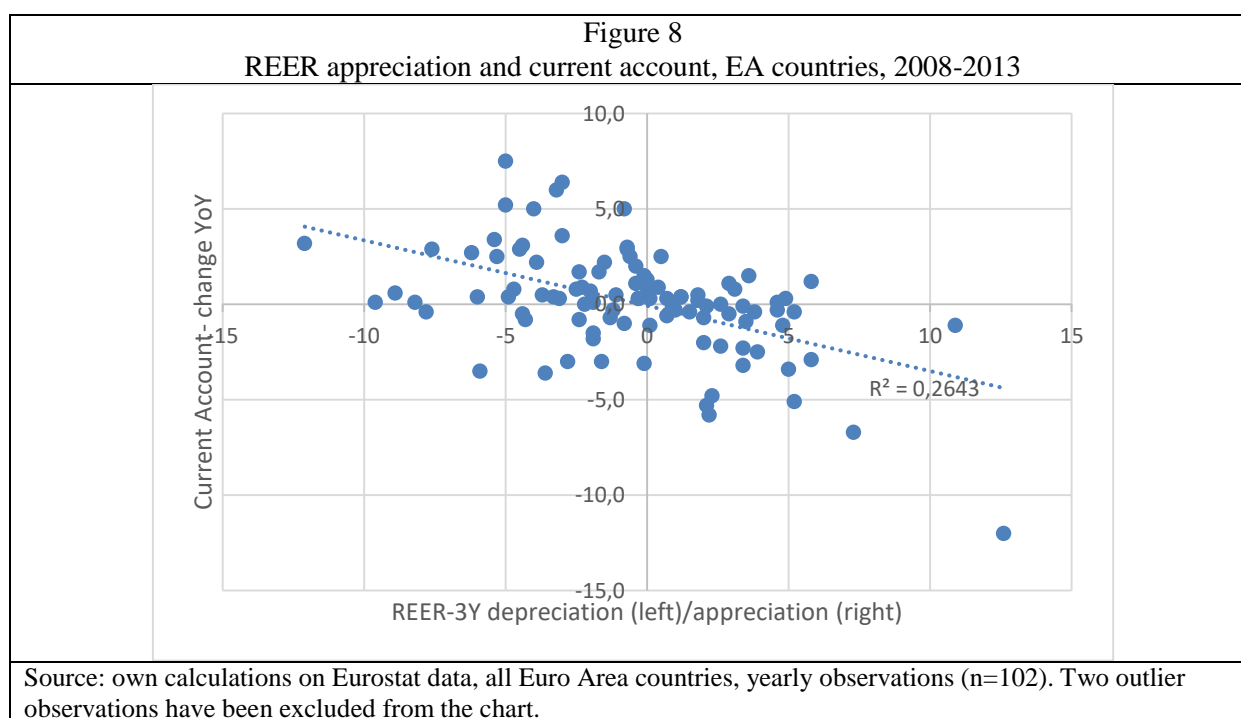
From this point of view, is worth noting (figure 7) that, when looking at the 11 major economies of the Eurozone, about 65% of GDP forecasts' "under-shooting"<sup>6</sup> episodes in the year 2011-2014 are matched by positive fiscal adjustments in respect to the previous year (quadrant 1). This seems to lend some weight

<sup>6</sup> GDP is considered as "undershooting" when it results below the forecasts published by the European Commission one semester before the end of the fiscal year.

to the Keynesian interpretation of a crisis led by excessive austerity, although nothing is said about whether a different course of action would have brought about better results. In fact, there is only one instance (Greece in 2014- quadrant 4) of “over-shooting” (GDP above forecasts) matched with a deteriorating fiscal stance.<sup>7</sup>

### 3.3 The Euro-design as original sin

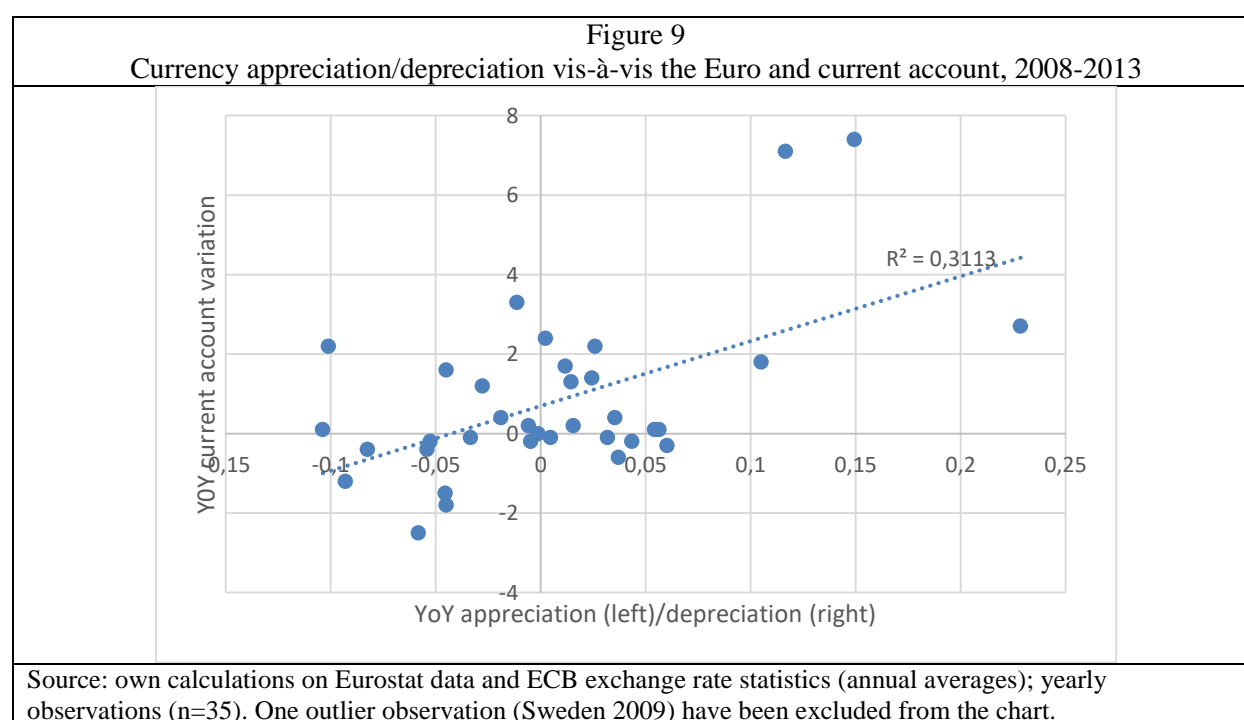
A last strand of thinking considers the establishing of the Euro as the fundamental cause of the crisis because, by removing exchange rates, it locked each country into a position where it borrows in foreign currency and cannot adjust the current account through exchange rate management (Stiglitz, 2015). This points especially to exchange rates (and the lack thereof). According to this view, the crisis was, to some extent, “unavoidable”. In the absence of a working exchange rate mechanism, any imbalance is to be equalized by relative prices adjustment, which is particularly hard to achieve provided that monetary policy is centralised under the control of a single central bank; the alternative is flexibilisation of the labour markets in order to provide real adjustment, and, to some extent, the fall in imports related with a decrease in GDP.



<sup>7</sup> We are interested, in particular, in quadrants 1 and 4 because they identify precise political decisions. Quadrant 2 and 3 are rather uninformative, because they collect instances of GDP and fiscal stance moving together, which is plausible given that the latter is, at least in part, endogenous to the former.

As shown in figure 8, indeed some degree of external adjustment has been achieved through Real Effective Exchange Rate depreciation/appreciation in the period 2008-2013.

Nevertheless, one may argue that exchange rate fluctuations, alone, would probably not have been able to provide the full extent of price adjustment needed, and some degree of fiscal integration would rather be needed to complement the real adjustment process. What happened then outside the Euro Area during the crisis? Figure 9 shows the correlation between change in the current account and the year-over-year depreciation/appreciation of the main non-euro area currencies vis-à-vis the Euro. The figure includes UK, SE, RO, BG, CZ, HU and PL, for a total of 35 observations. Although, as expected, there is some correlation between exchange rate depreciation and amelioration of the current account, the  $R^2$  associated with currency depreciation is only very slightly larger than the  $R^2$  associated with internal devaluations for Euro-Area countries. Proponents of the “original sin” thesis seem to believe that, while –in principle- adjustment may be achieved through internal devaluations, this is comparably less effective, politically costlier, and economically under-performing in respect to the simple adjustment on the currency denomination side.



Finally, a “moderate” variant of the previous narrative states that the endurance of the crisis was mainly due to the wrong Eurozone institutional design when the crisis struck, and to the delay in providing credible institutional response in a timely fashion. In particular, the Eurozone design holds a direct responsibility because of its lack of common stabilization instruments. At least one option (either a fiscal union, a full-fledged banking union, or a proper lender of last resort) was needed (Merler & Pisani-Ferry, 2012b).. In the absence of a full-fledged fiscal union, of a banking union, and of a lender of last resort, and in presence of low labour mobility, adjustment would be mediated exclusively by relative prices adjustment in the tradable sector, which may turn out to be politically and economically hard to sustain for prolonged periods of time (De Grauwe, 2007).<sup>8</sup>

In sum, several of the positions reconstructed in the previous paragraphs are overall linked with OCA theory and imply that the crisis had in fact at least a partially endogenous dimension, thus confirming the functional crisis hypothesis. Others tend to de-emphasize the institutional reasons of the crisis, blaming instead a wrong policy mix enacted domestically and/or at European level prior to and during the crisis. While consistent differences exist between the various interpretations of the crisis, a recent attempt by a pool of leading economists has contributed to forge a general narrative encompassing many, although not all, the arguments put forward in this analysis (Baldwin et al, 2015).

The “consensus narrative”, as it is called by the sixteen authors, interprets the crisis as having a common root: the excessive capital flows between Euro countries that boosted non-productive consumption, thus rising inflation and hampering competitiveness in recipient countries. When the crisis hit, the excess lending generated an outflow of capitals which required the sovereign to step in in order to prevent a generalized bank collapse, considerably worsening public finances. Then, the absence of a proper lender of last resort made the residual banks (who had lent to the governments) vulnerable to the rising interest rates on government bonds. While this narrative is coherent and fascinating, it tends to play down the accumulation

---

<sup>8</sup> Chapter 7 analyses with a great deal of detail the consequences of the failure to return to sustained growth on the electoral performance of Eurosceptic parties, which -according with a functional theory of legitimacy, developed in chapter 5- is mainly dependent on the performance-driven output legitimacy as long as proper democratic institutions are not established.

of public and private debt stocks before the crisis, and –differently from Merler and Pisani-Ferry (2012b)- tends to emphasize, in particular, the lack of a proper lender of last resort the main flaw of the Eurozone design. Nevertheless, the “consensus narrative” proposed by Baldwin et al. (2015) points in the direction of a partial functional explanation of the crisis: therefore, the next sections of this paper attempt to shed light on the determinants of the crisis, in order to address our key question on whether it is possible to establish the functional nature of the crisis. At this regard, the functional crisis hypothesis is considered as confirmed if (1) a clear endogeneity of the crisis is found, and/or (2) only partial endogeneity is found, but the intensity of the crisis is found being correlated with institutional improvements predicted by one of the theories. In other words, consistently with the functional clock framework from Schmitter:

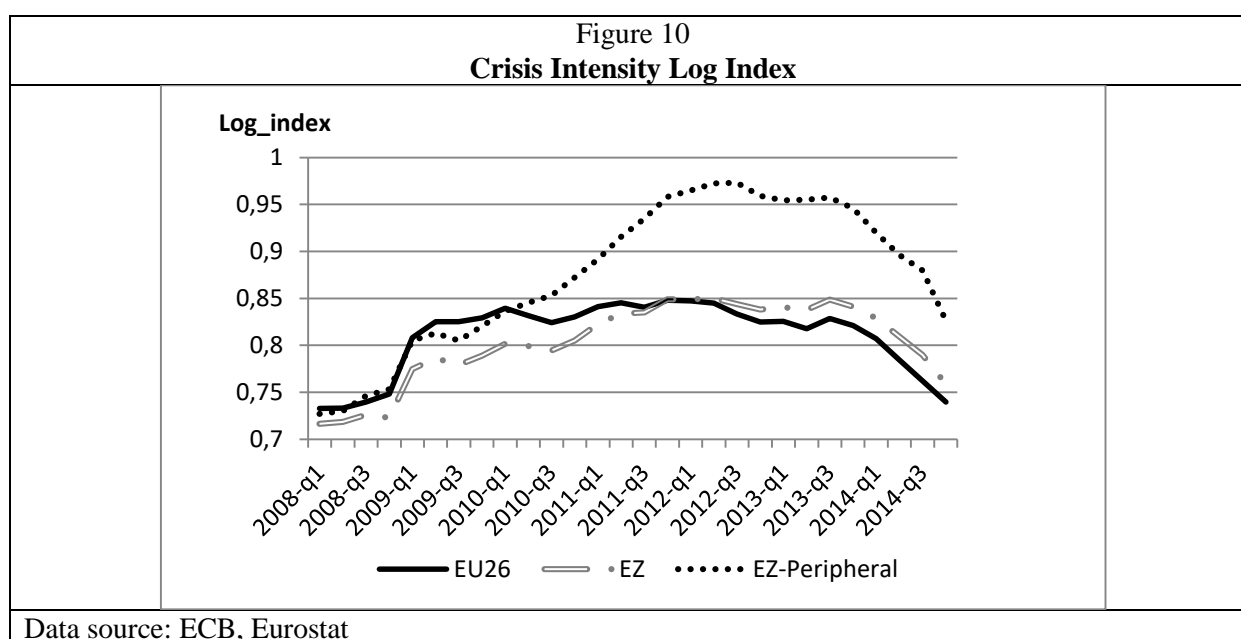
- (1) If a fully endogenous crisis is solved without a re-arrangement of competences, the Union has successfully encapsulated its crisis.
- (2) If a fully exogenous crisis is solved without a re-arrangement of competences, then it is not a functional crisis as defined in this work.
- (3) if a crisis (endogenous or exogenous) is not solved, but one of the survey theories prescribes that it would be solved if the competences were re-arranged, then the judgement must be suspended.
- It follows that (4) backward induction is adopted in the case of “partially endogenous” crises. In fact, if the crisis was exogenous in its origins, but the reallocation of competences solved it, then it was (in fact) partially endogenous, because if those competences were differently organised in the first place, reaction (2) would have happened instead.

## 4. Variables

### *4.1. Redefining the Eurocrisis as dependent variable: a simple composite index*

Investigating the determinants of the Eurocrisis through econometric analysis requires a specific definition of the crisis itself that is both sufficiently simple to fit in a panel data model, and complex enough to capture the different aspects of the crisis. In fact, the overarching divergence of views presented in the previous paragraph is the result of a complex debate that has shifted along with the crisis itself. Yet, seven years on, finding a satisfactory definition of a multidimensional crisis is increasingly complex. In fact, depending on

which indications one takes into consideration, the conclusion can be drawn that the crisis has ended since years, as much as that it has just moved beyond its worst moment but it is far from over. If one looks at interest rates on public bonds, for instance, Draghi's "whatever it takes" speech and the ensuing OMT and Quantitative Easing programmes have sufficiently curbed borrowing costs for all Eurozone countries but Greece to levels comparable, if not below, the pre-crisis average.



On the other hand, if one looks at unemployment or total real GDP figures, a handful of countries, including Italy, France and Spain, are yet to recover to their respective 2007 levels. Unemployment is particularly worrisome because of its striking social and political implications; in Chapter 7 (also Nicoli, 2016) it is shown that a strong relationship between duration of high levels of unemployment and support for Eurosceptic parties in elections exists, Euroscepticism being in turn one of the major forces preventing a swift implementation of a fiscal integration agenda at EU level; this "circular illness" of the integration process is also discussed in Chapter 5.

In fact, I believe that a narrow focus on either indicator is misleading; both the socio-economic dimension (captured by unemployment rate) and the financial stability dimension (proxied by the interest rate) are important. I therefore propose a crisis composite indicator in which both aspects of the Eurocrisis appear on equal footing. In building the crisis indicator I generally follow the prescriptions of OECD (2008) and

the European Commission (2014) guides on building composite indicators, although the presence of only two dimensions largely simplifies the required procedures. At this regard I collected unemployment and interest rates data for 26 European countries over 28 quarters (from Q1-2008 to Q4-2014) for a total of 728 observations, building several variants of the composite index. As we aim to explain possible determinants of the composite indicator, it is handy that the correlation between the two variables is positive and small (0.47). Standard theory generally excludes direct channels of influence between the two variables, with the exception of public expenditure (which is affected by interest rates and affects unemployment)<sup>9</sup>; the correlation is probably due to common determinants, which simplifies our analysis. Figure 10 reports the evolution of the composite index (in log scale) by geographical areas.

#### 4.2. Seeking for the Eurocrisis' determinants: the independent variables

As shown in the previous paragraphs, there is no shortage of points of view on the possible determinants of the Eurocrisis. The list of independent variables operationalized in this chapter builds largely on the existing literature. The independent variables under scrutiny can be clustered in five broad groups. Table 1 collects all relevant information concerning the independent variables used in the several specifications.

##### - *Pre-crisis economic variables*

Previous paragraphs have shown that a substantial amount of scholarly work has focused on imbalances among peripheral and core member states grown before the crisis. A first set of time-invariant independent variables attempts to catch these effects. *Avg\_construction\_GDP* captures the average 2002-2007 size of the construction sector over GDP. *Avg\_ExternalBalance* points at the average yearly surplus or deficit over the same period; *deltaTOTALdebt*, *deltaPRIVATEdebt*, and *deltaPUBLICdebt* compute, over the same period, the cumulative increase or decrease in total, private, and public debt expressed in GDP shares; *PrecrisisPRIVATEdebt*, *PrecrisisPUBLICdebt*, and *PrecrisisTOTALdebt* report the absolute level of private, public and total debt in 2007; *PrecrisisLabourCosts* measures the increase in labour costs in

---

<sup>9</sup> The idea that higher public bond yields, constraining the government capacity of spending, do fuel short-term unemployment, belongs to the classical paradigm of Keynesian economics and is generally being supported by the advocates of anti-austerity measures. It is controversial, however, whether in the long run unemployment is moderated by public spending. For instance, Fedeli, Forte and Ricchi (2013) find substantial evidence in support of the opposite thesis, namely that deficit spending increases long-term unemployment.

industry and services, expressed in 2005 index, from 2001 to 2008; *PrecrisisREER* measures the change in the Real Effective Exchange Rate from 2001 to 2008. Data have been, in general, obtained from Eurostat. Most of these variables have been interacted with the dummy variable *Euromembership* in the attempt to find out whether specific effects of adoption of the single currency have appeared through these channels, as suggested in parts of the literature.

- *Economic performance during the crisis*

A second subset of independent variables looks at specific economic performance during the crisis. The major risk associated with this subset of variables is, in fact, endogeneity: the crisis, in its social and financial components captured by the composite indicator in use, may be influenced, but also influence, certain variables one would account for. *QuarterlyGDP* shows the evolution of quarterly GDP data from 2008Q1 and 2014Q4, but might produce endogeneity-related issues. *QuarterlyCurrentAccount* reproduces the evolution of the current account of the concerned countries, in the attempt to describe its external performance; *LabourCosts\_Industry* indicates the evolution of the quarterly labour cost index with 2012 as a base year; *REER\_1l* indicates the change in the Real Effective Exchange Rate, lagged one year; finally, we also account for *QuarterlyDeficit*, although a degree of endogeneity may be present considering that the dependent variable includes interest rates on public bonds, which affect (and are affected by) deficit expenditure.

- *Governance and institutional factors during the crisis*

In the years of the crisis an intense wave of new policies, institutions and procedures has been put forward in the attempt to moderate its effects. The institutional changes brought about during the crisis have been modelled through a series of dummy variables. More in detail, *EuropeanSemester* captures, from 2011, the introduction of the general framework of the new economic governance; *TwoPack* refers to its first reform, entered into force in March 2013; *ESMapproved* refers to the approval of the European Stability Mechanism, while *ESMentranceintoforce* indicates the starting date of its operations; *TSGP* indicates the date of agreement on the Treaty On Stability, Coordination and Governance. The variable *incrementalFiscalGovernance*, finally, catches the incremental nature of the European fiscal governance.



On financial and banking governance, four variables have been identified: *EUBankAuthority* indicates the creation of the European Banking Authority in 2011; *BankingUnion\_CS* indicates the agreement on the first pillar of the European Banking Union, the Common Supervision, while *BankingUnion\_CR* indicates the second pillar, the common resolution agreement; finally, *incrementalBankingUnion* catches the incremental nature of the European financial governance. An alternative, comprehensive measure of the cumulative changes in governance is given by *EURII*, a normalized version of the European Regional Integration Index developed by the ECB (2015). *ECBrate* indicates in each quarter the average Main Refinancing Operations Rate set by the ECB; *FinancialAidAgreed* indicates the total amount of financial aid agreed for each country in a given quarter; *CumulativeFinancialAid* indicates the total sum effectively delivered to a country over time; *FinancialAidFirepower* indicates the total amount of money pooled in ad-hoc international financial institutions of European inception (excluding therefore the IMF, despite it intervened in each EU bailout so far). Finally, *OMT* indicates the effects of the ECB communication strategy put in place by the ECB President, Mario Draghi, in June 2012.

Table 1 -list of IVs

Independent Variable	Description	Data source	notes
(1) avg_construction_gdp	2001-2007 average GPD share of the Construction sector	Eurostat	
(2) avg_ExternalBalance	2001-2007 average Current Account surplus/deficit in % of 2008 GDP	Eurostat	
(3) quarterlyDeficit	Quarterly fiscal surplus/deficit, % of quarterly GDP	Eurostat	
(4) QuarterlyCurrentAccount	Quarterly Current Account surplus/deficit, % of quarterly GDP	Eurostat	
(5) labourCosts_BUSINESS	Labour Costs Index, quarterly data (2012=100)	Eurostat	
(6) PrecrisisLabourCosts	Difference in the Labour Costs Index 2008-Q2 minus 2001-Q1 (2001=100)	Eurostat	Rescaled from original index
(7) PreCrisisPRIVATEdebt	2008 private debt as % of 2008 GDP	Eurostat	
(8) DELTAdebtPRIVATE	Increase/decrease in private debt, 2001-2008, % of GDP	Eurostat	Our calculations on Eurostat data
(9) PreCrisisPUBLICdebt	2008 public debt as % of 2008 GDP	Eurostat	
(10) DELTAdebtPUBLIC	Increase/decrease in public debt, 2001-2008, % of GDP	Eurostat	Our calculations on Eurostat data
(11) PreCrisisTOTALdebt	2008 public+private debt as % of 2008 GDP	Eurostat	Our calculations on Eurostat data
(12) DELTAdebtTOTAL	Increase/decrease in public+private debt, 2001-2008, % of GDP	Eurostat	Our calculations on Eurostat data
(13) OMT	Dummy variable indicating the entrance into force of the ECB OMT programme	ECB	1 from Q3-2012 onwards
(14) lenderOfLastResort	Dummy variable for the presence of a lender of last resort for Sovereign		1 from non-Eurozone member states, 1 for Eurozone Member states from Q3-2012 onwards
(15) ECBrate	Main Refinancing Operations lending rate of the ECB	ECB	Quarterly averages weighted for number of days
(16) REERt_1	Real Effective Exchange Rate index in the previous quarter	Eurostat	
(17) PrecrisisDeltaREER	Difference in the REER index 2008-Q2 minus 2001-Q1 (2001=100)	Eurostat	
(18) European_Semester	Dummy variable indicating the approval of the European Semester	European Commission	1 from Q4-2011 onwards
(19) Two_Pack	Dummy variable indicating the approval of the Two-Pack	European Commission	1 from Q2-2013 onwards
(20) TSGP	Dummy variable indicating the approval of the Fiscal Compact	European Commission	1 from Q1-2013 onwards
(21) ESMapproved	Dummy variable indicating the approval of the ESM	European Commission	1 from Q2-2011 onwards
(22) ESMentryintoforce	Dummy variable indicating the entry into force of the ESM	European Commission	1 from Q2-2012 onwards
(23) EubankAuthority	Dummy variable indicating the creation of the EBA	EBA	1 from Q1-2011 onwards
(24) Banking Union_CS	Dummy variable indicating the approval of the first pillar of the Banking Union	European Commission	From Q2-2013 onwards
(25) Banking Union_CR	Dummy variable indicating the approval of the second pillar of the Banking Union	European Commission	From Q2-2014 onwards

(26)	IncrementalFiscalGovernance	Incremental count variable for fiscal governance		Adds 1 after each of the previous fiscal governance measures is introduced
(27)	IncrementalBankingUnion	Incremental count variable for banking union		Adds 1 after each of the previous banking governance measures is introduced
(28)	EURII	European Regional Integration Index	ECB (2015)	Normalized to 2010=1
(29)	FinancialAidFirepower	Total maximal bailout capacity of EU anti-crisis funds (EFSF, EFSM, ESM)	European Commission	
(30)	FinancialAidagreed	Amount of financial aid agreed for a given country	European Commission, IMF	
(31)	CumulativeFinancialAid	Cumulative sum of financial aid effectively delivered to a given country	European Commission, IMF	Our computations
(32)	EURextPosition	Interaction variable between (2) and (44)		
(33)	EURavgConstruction	Interaction variable between (1) and (44)		
(34)	EURdeltaPublicDebt	Interaction variable between (9) and (44)		
(35)	EURdeltaTotalDebt	Interaction variable between (11) and (44)		
(36)	EURdeltaPrivateDebt	Interaction variable between (8) and (44)		
(37)	EURprivateDebt	Interaction variable between (7) and (44)		
(38)	EURpublicDebt	Interaction variable between (9) and (44)		
(39)	EURtotalDebt	Interaction variable between (11) and (44)		
(40)	EURlabourCosts	Interaction variable between (5) and (44)		
(41)	EURpreCrisisLabourCosts	Interaction variable between (6) and (44)		
(42)	EURdeficit	Interaction variable between (3) and (46)		
(43)	Eumeetings	Number of European Council and Euro Area Summit meetings in the quarter	European Council	
(44)	PrecrisisEuromembership	Dummy variable indicating pre-crisis Euro Area membership		1 if the country joined the EZ before 2008
(45)	NewMemberstate	Dummy variable for new member states		1 if the country accessed the EU between 2004 and 2007
(46)	Euromembership	Dummy variable indicating membership of the EMU		1 from the moment the country adopts the Euro
(47)	Peripheral	Dummy variable indicating countries on the southern and eastern border		1 if the country is a Mediterranean or Eastern country
(48)	Nationalelection	Dummy variable indicating that a national election took place in the quarter	Nicoli (2016)	
(49)	Europeanelection	Dummy variable indicating that European Parliament elections took place in the quarter	European Parliament	

- *Euro Area specific variables*

Several of the approaches explained in the previous paragraphs either assumed that the simple Euro Area membership had contributed to the crisis, or that certain domestic elements of weakness, given the particular condition of monetary union countries, have played a significant role in the crisis. Therefore, several variables have been interacted with the dummy *Euromembership* in the attempt to find out if any of such effects have existed in practice. This concerns, more specifically, *EURexternalPosition*, *EURaverageConstruction*, *EURdeltaPublicDebt*, *EURdeltaPrivateDebt*, *EURdeltaTotalDebt*, *EURprivateDebt*, *EURpublicDebt*, *EURtotalDebt*, *EURquarterlyDeficit*, *EURlabourCosts* and *EURpreCrisisLabourCosts*.

- *Control variables*

Finally, the last group of IVs included in this study is a set of control variables useful to better catch heterogeneity across the panels. *Euromembership*, in particular, is treated as a control variable because we would rather assume that, if an effect of Eurozone membership indeed exists, is it likely mediated by one

of the economic variables coupled with membership.<sup>10</sup> Furthermore, we control for *NewMemberState*, indicating the member countries which joined the EU in the 2004 and 2007 enlargements, and *Pheripheral*, indicating Mediterranean countries. Finally, we also control for politically relevant events, like *NationalElections*, *EuropeanElections*, and *EUMeetings*.<sup>11</sup>

## 5. Methodology and Model

### 5.1. Methodology

How to identify whether a specific effect of Euro Area membership indeed existed during the Eurocrisis? Two alternative testing strategies have been considered. First, one could look separately at the two subsets of pre-crisis Eurozone and non-Eurozone members (the former counting about 420 observations and the latter counting about 310 observations) and then compare the regression results across specifications to find whether the Eurozone membership played a role. Second, one could merge all observations in a larger, single dataset and use interaction variables to extrapolate certain group specific effects.

The first approach (A) requires to separate the database into two subgroups along with each country's Euro Area membership. For obvious reasons, this approach excludes any interaction variable with Eurozone membership from the analysis. The main advantage of this approach is that, by separately testing the two groups, the need of interaction variables is eliminated, avoiding risks of multicollinearity. However, by doing so, we greatly reduce the number of observations upon which the regressions are performed, and we might also lose part of the explanatory power of certain variables which could fail to be statistically significant in the groups separately but could turn significant once the groups are pooled.

The general hypothesis, in this first methodological approach, is that (H.A.1) *the coefficients of the statistically-significant variables tend to be larger in the Euro group, rather than in the non-Euro group.*

---

<sup>10</sup> Moreover, provided that *Euromembership* is a binary variable, we expect its coefficient to be negative, because several countries joined the Euro Area during or after the crisis, when their economic condition was considerably ameliorated- this is the case of the three Baltic countries, that largely suffered from the crisis. Because other economic effects are captured by appropriate variables, the *Euromembership* effect is likely inversely correlated with the crisis indicator.

<sup>11</sup> Although standard EU Council meetings are also events of relevant political nature and might have played a substantial role during the crisis, they have occurred at least on a quarterly basis since 1996. As our dataset is built on quarterly data, the effect of each ordinary meeting cannot be accounted for through a simple dummy.

More in detail, we also expect (H.A.2) to find statistical evidence of the importance of governance and OMT programmes. Finally, finding significance of the construction share of the GDP and on private debt would lend further credibility to the “consensus narrative” discussed above; in a lesser measure, current account and labour costs would also point into that direction, although relevance of these effects is also shared by supporters of the “domestic performance” argument, along with public debt accumulation. Finally, if economic variables are statistically relevant only in the Euro group, or if only governance variables and lender of last resort-related variables are significant, the “Euro Area original sin” explanation would find support.

The second approach (B) makes use of the full dataset merging Euro Area and non-Euro Area countries in one single regression, and recurring to interaction variables between Euro Area membership and the economic regressors of interest. The benefits of this approach are twofold. On the one hand, we fully exploit the database, substantially increasing the number of observations and likely obtaining more precise estimations. On the other hand, some regressors which might fail to be statistically significant when the database is split may turn out to be significant in a larger database. The main limitation of this approach is that the economic meaning of the effect of Euro membership interaction variables might be controversial, especially if a degree of collinearity were to emerge by multiplying *Euromembership* (which is a dummy variable) and the economic regressors. This concern notwithstanding, I put forward two hypotheses in approach B. First, (H.B.1) *I expect to see a statistically significant impact of pre-crisis economic performance*. Second, (H.B.2) *I expect to see certain interaction variables (i) to be statistically significant and (ii) to produce a stronger effect on the Euro Area countries*. In term of specific effects of given variables, the same discussion presented in the previous paragraph applies, although the “Euro Area original sin” would find support if only the interaction variables, but not the original regressors, turn out to be statistically significant.

## 5.2. Model

The data collected cover 28 quarters from January 2008 to December 2014, for a total of 728 observations. The data structure invites for a choice between Pooled OLS Regression with panel-robust standard errors, Fixed Effects (FE) and Random Effects (RE). Additional options are offered by the Hausman-Taylor (H-

T) regression and by panel-corrected standard errors in OLS. Our preference goes out to a RE model because several of the variables of interest are time-invariant variables catching the situation of the countries before the crisis. When consistent with the hypothesis that panel-specific errors are not correlated with the regressors, RE estimates are reported in this panel. While perfect independence is rarely achieved, including sufficient variables to decrease heterogeneity could help in reducing the magnitude of the bias. The random effects model is tested against the fixed-effects alternative through a Hausman specification test. When consistent with Hausman test results, the random effects estimates are reported.<sup>12</sup> In this regard, we opted for a random-effects model which specifies various country-specific factors in the right-end of the equation to minimize the risk of omitted variable bias. If Random Effects is rejected, a mixed approach using the H-T is our second best choice, as it allows for estimating fixed effects while adding to the model time-invariant regressors estimated consistently with a RE model.

Several different specifications were tested, in both approaches described in paragraph 4.3. Equation 1 recalls the values for the baseline specification in approach A (A1 Euro and A1 Non-Euro). The main difference in the baseline specification is that non-Euro area countries lack the  $\beta_{14}OMT_t$  Euro-Area specific variable, but show instead the  $\beta_{14}LenderOfLastResort_{it}$  dummy variable, which is positive for all countries except for countries that joined the Euro Area during the crisis.

$$(1) \text{INDEXeuro}_{it} = \beta_0 + \beta_1 \text{ConstructionGDP}_i + \beta_2 \text{ExternalBalance}_i + \beta_3 \text{QuarterlyCurrentAccount}_{it} + \beta_5 \text{LabourCosts}_{it} + \beta_6 \text{PrecrisisLabourCosts}_i + \beta_7 \text{DeltaDebtPrivate}_i + \beta_8 \text{PrecrisisDebtPrivate}_i + \beta_9 \text{PrecrisisPublicDebt}_i + \beta_{10} \text{DeltaDebtPublic}_i + \beta_{11} \text{IncrementalFiscalGovernance}_t + \beta_{12} \text{IncrementalBankingUnion}_t + \beta_{13} \text{FinancialAidFirepower}_t + \beta_{14} OMT_t + \beta_{15} \text{NewMemberstate}_i + \beta_{16} \text{peripheral}_i + \beta_{17} \text{NationalElection}_{it} + \beta_{18} \text{EuropeanElection}_{it} u_i + \varepsilon_{it}$$

Three more specifications were tested in the comparative approach: Specification A2 includes only private debt, specification A3 includes only public debt, and specification A4 uses Real Effective Exchange Rate

<sup>12</sup> To deal with potential heteroskedasticity, robust standard errors should be adopted. However, the standard version of the Hausman test requires homoskedasticity assumption. To deal with potential heteroskedasticity, we decided to proceed with a double testing approach, using two alternatives: the standard Hausman test and the auxiliary regression procedure proposed by Woolridge (2010) and Mundlack (1978). This is operationalised through the `xtoverid` command in Stata and allows for panel-robust standard Errors.

measures  $(\beta_{18}REER_{t-1,i} + \beta_{19}PreCrisisDeltaREER_{it})$  instead of labour cost indexes. While the Euro Area group passed the robust version of the Hausman test in all specifications with margin,<sup>13</sup> the non-Euro group consistently failed to do so; at this regard, the specifications for the non-Euro Area group have been estimated through Hausman-Taylor regression in order to maintain a meaningful comparison between the two groups, which would otherwise would have been impossible as the Fixed Effects model would have ruled out any time-invariant IV. The results for all Specifications are shown in table 3. In contrast, the pooled approach counts an enlarged set of variables to account for Euro Area specific effects as well as for further profiling of individual countries. Equation 2 recalls the baseline specification for approach B (specification B1):

$$(2) INDEX_{it} = \beta_0 + \beta_1 ConstructionGDP_i + \beta_2 ExternalBalance_i + \beta_3 QuarterlyCurrentAccount_{it} + \beta_5 LabourCosts_{it} + \beta_6 PrecrisisLabourCosts_i + \beta_7 DeltaDebtPrivate_i + \beta_8 PrecrisisDebtPrivate_i + \beta_9 PrecrisisPublicDebt_i + \beta_{10} DeltaDebtPublic_i + \beta_{11} IncrementalFiscalGovernance_t + \beta_{12} IncrementalBankingUnion_t + \beta_{13} FinancialAidFirepower_t + \beta_{14} OMT_t + \beta_{15} EuroExternalBalance_i + \beta_{16} EuroLabourCosts_{it} + \beta_{17} EuroPrecrisisLabourCosts_i + \beta_{18} EuroDeltaDebtPrivate_i + \beta_{19} EuroDeltaDebtPublic_i + \beta_{20} EuroPrecrisisDebtPrivate_i + \beta_{21} EuroPrecrisisDebtPublic_i + \beta_{22} NewMemberstate_i + \beta_{23} peripheral_i + \beta_{24} NationalElection_{it} + \beta_{25} EuropeanElection_{it} + u_i + \varepsilon_{it}$$

As in the previous case, several more specifications were tested (B2, B3, B4, B5 and B6). Specification B2 removed from the regression the interaction factors which have no strong support in the literature, namely  $\beta_{18}EuroDeltaDebtPrivate_i$  and  $\beta_{20}EuroPrecrisisDebtPrivate_i$ ; the credit boom-and-boost circle, in fact, is supposed to affect the whole European Union (including countries such as UK for instance) because of free circulation of capital and not being restricted to the EMU countries.

Specification B3 removes  $\beta_9 PrecrisisPublicDebt_i$ ,  $\beta_{10} DeltaDebtPublic_i$ ,  $\beta_{19} EuroDeltaDebtPublic_i$  and  $\beta_{21} EuroPrecrisisDebtPublic_i$  from the regression; Specification B4 does the same with Private debt. Specification B5, in addition exchanges  $\beta_5 LabourCosts_{it}$  and  $\beta_6 PrecrisisLabourCosts_i$  with  $\beta_{18} REER_{t-1,i}$  and  $\beta_{19} PreCrisisDeltaREER_{it}$  (the same applies to the transformed Euro versions).

<sup>13</sup> The Euro Area group safely passed the augmented regression test for robust standard errors implemented through *xtoverid* for all specifications but A4, with p- values ranging from 0.25 to 0.09.

Specification B6 removes  $\beta_{11}IncrementalFiscalGovernance_t$  and  $\beta_{12}IncrementalBankingUnion_t$  exchanging it with the full list of specific governance indicators (variables No. 18-25 in Table 1). The results for all specifications are shown in Table 4.

## 6. Results

I will first proceed in analysing the results yielded by the comparative approach, focusing on the outcome of the different specifications in the attempt to identify the leading causes of the evolution of our composite crisis indicator. Second, I will compare the specific coefficients in the specifications of interest across the two groups to assess whether a Eurozone effect does indeed emerge. Likewise, in the pooled approach we focus in particular on the interaction terms between pre-crisis Eurozone membership and the economic variables of interest.

### 6.1. Comparative approach

Four specifications were tested in the comparative approach: results are shown in table 2. The first three specifications include only private debt (A2), only public debt (A3), or both (A1), and the last one (A4) uses Real Effective Exchange Rates (REERs) instead of labour costs. The augmented Hausman Test was consistently passed in the Eurozone Group in specifications A1-A3, but failed in specification A4. The non-Eurozone group never passed the augmented Hausman Test.

However, as fixed effects is not suitable for the comparison given the relevance of time-invariant variables included in the regression, it was opted to compare the RE estimator results for the Euro Area countries with H-T estimations for non-Euro Area countries, in which time-invariant IVs are estimated through RE, and time-varying IVs are estimated with FE. Specification 4 is, by far, the least interesting: substituting labour costs with REER Indexes does not yield additional information as both the pre-crisis REER index and the lagged REER index fail to be statistically significant and prevent application of RE estimations. Pre-crisis labour costs, instead, are consistently statistically significant for the Euro Area group across specifications A1-A3; the same applies to the pre-crisis external balance.

As expected, the pre-crisis external balance is negatively correlated with the crisis indicator, suggesting that countries failing to accumulate an external surplus in the pre-crisis period experienced worse conditions

during the crisis years; likely due to the sudden capital outflows occurred both in the early phase of the global crisis and after 2011 (Merler and Pisani-Ferry 2012a; Baldwin et al, 2015). This negative correlation between pre-crisis current account surpluses and crisis indicator points as well in the direction of deteriorating competitiveness as a driver for the Eurocrisis, as suggested by the Commission and others. One shall notice, however, that these effects -related to both deteriorating competitiveness and unrestricted capital outflows- appear to be consistently stronger for the Euro Area group across all specifications. The coefficient  $\beta_2$  for *ExternalBalance* is, on average across specifications A1-A3, 35% larger in the Euro Area group (27% in specification A1 when both private debt and public debt are included, 37% in A2 when only private debt is included, 40% in A3 when only public debt is accounted).

Moreover, pre-crisis labour costs are positively correlated with the crisis indicators: as suggested by previous literature, the loss of competitiveness before the crisis is mirrored in the economic performance of the countries during the crisis. This, however, is especially valid for Euro Area countries: significant at 1% level for the Euro Area group in specification A1, and at 5% level in specifications A2 and A3; they however fail to be significant in the non-Euro area group for specifications A1 and A2. When private debt is not accounted for (A3) pre-crisis labour costs appear to be significant also in the non-Euro group at the 5% level, but  $\beta_6$  for the non-Euro Area group is about 11 times smaller for the non-Euro Area group ( $\beta_{6,Euro} = 5.84$ ;  $\beta_{6,NonEuro} = 0.54$ ). Differently from what predicted by the “consensus view” (Baldwin et al., 2015) the comparative approach fails to consistently indicate construction share of GDP and debt accumulation (both private and public) as drivers of the crisis.

Table 2- Approach A, Comparative

	A1		A2		A3		A4	
	Euro	Non Euro	Euro	Non Euro	Euro	Non Euro	Euro	Non Euro
avg_construction_gdp	0.238 (0.47)	0.296 (0.54)	0.351 (1.09)	-0.238 (0.56)	0.200 (0.57)	<b>0.469</b> <b>(1.70)*</b>	0.315 (0.41)	0.037 (0.26)
ExternalBalance	<b>-0.393</b> <b>(2.29)**</b>	<b>-0.309</b> <b>(2.73)***</b>	<b>-0.397</b> <b>(3.38)***</b>	<b>-0.290</b> <b>(2.99)***</b>	<b>-0.379</b> <b>(2.73)***</b>	<b>-0.272</b> <b>(3.61)***</b>	<b>-0.535</b> <b>(2.73)***</b>	<b>-0.297</b> <b>(8.86)***</b>
QuarterlyCurrentAccount	<b>0.139</b> <b>(2.69)***</b>	<b>0.176</b> <b>(13.23)***</b>	<b>0.137</b> <b>(2.70)***</b>	<b>0.176</b> <b>(13.31)***</b>	<b>0.138</b> <b>(2.72)***</b>	<b>0.176</b> <b>(13.40)***</b>	<b>0.154</b> <b>(2.57)**</b>	<b>0.171</b> <b>(13.14)***</b>
labourCosts	<b>-4.484</b> <b>(1.66)*</b>	<b>-1.408</b> <b>(3.38)***</b>	<b>-4.580</b> <b>(1.70)*</b>	<b>-1.521</b> <b>(3.67)***</b>	<b>-4.473</b> <b>(1.68)*</b>	<b>-1.423</b> <b>(3.43)***</b>		
PreCrisisLabourCosts	<b>5.840</b> <b>(2.69)***</b>	0.410 (1.03)	<b>5.549</b> <b>(2.53)**</b>	0.200 (0.64)	<b>5.846</b> <b>(2.37)**</b>	<b>0.547</b> <b>(2.24)**</b>		
PreCrisisPrivateDebt	0.001 (0.13)	-0.012 (0.31)	-0.002 (0.32)	-0.033 (0.95)			-0.000 (0.01)	-0.001 (0.15)
DeltaDebtPrivate	0.022 (1.55)	-0.009 (0.28)	<b>0.022</b> <b>(2.50)**</b>	0.001 (0.06)			0.029 (1.21)	<b>-0.053</b> <b>(3.93)***</b>



PreCrisisPublicDebt	0.011 (0.52)	0.049 (1.62)			-0.002 (0.12)	<b>0.048</b> <b>(1.76)*</b>	0.012 (0.32)	<b>0.103</b> <b>(9.04)***</b>
DeltaDebtPublic	-0.043 (0.91)	-0.036 (0.83)			<b>-0.063</b> <b>(1.76)*</b>	-0.023 (0.93)	-0.051 (0.64)	<b>-0.130</b> <b>(6.86)***</b>
OMT	<b>-0.634</b> <b>(1.86)*</b>		<b>-0.629</b> <b>(1.87)*</b>		<b>-0.632</b> <b>(1.87)*</b>		-0.596 (1.64)	
LenderOfLastResort		<b>-1.966</b> <b>(7.13)***</b>		<b>-1.958</b> <b>(7.28)***</b>		<b>-1.988</b> <b>(7.51)***</b>		<b>-2.090</b> <b>(8.40)***</b>
incrementalgovernance_fiscal	<b>0.180</b> <b>(2.25)**</b>	<b>-0.141</b> <b>(1.69)*</b>	<b>0.180</b> <b>(2.26)**</b>	<b>-0.138</b> <b>(1.67)*</b>	<b>0.180</b> <b>(2.25)**</b>	<b>-0.139</b> <b>(1.68)*</b>	<b>0.192</b> <b>(2.21)**</b>	<b>-0.165</b> <b>(1.97)**</b>
incrementalBankingUnion	<b>-0.492</b> <b>(2.79)***</b>	<b>-0.472</b> <b>(2.95)***</b>	<b>-0.490</b> <b>(2.80)***</b>	<b>-0.466</b> <b>(2.92)***</b>	<b>-0.491</b> <b>(2.80)***</b>	<b>-0.473</b> <b>(2.96)***</b>	<b>-0.572</b> <b>(2.80)***</b>	<b>-0.557</b> <b>(3.48)***</b>
FinancialAidFirepower	<b>0.003</b> <b>(2.01)**</b>	<b>0.001</b> <b>(3.74)***</b>	<b>0.003</b> <b>(2.02)**</b>	<b>0.001</b> <b>(3.81)***</b>	<b>0.003</b> <b>(2.02)**</b>	<b>0.001</b> <b>(3.76)***</b>	<b>0.002</b> <b>(1.73)*</b>	<b>0.001</b> <b>(3.21)***</b>
NewMemberstate	<b>-3.040</b> <b>(1.99)**</b>	-1.411 (0.28)	<b>-2.753</b> <b>(4.90)***</b>	-3.610 (0.82)	<b>-4.470</b> <b>(4.88)***</b>	0.392 (0.52)	<b>-3.350</b> <b>(1.67)*</b>	<b>2.384</b> <b>(2.05)**</b>
Peripheral	-0.148 (0.13)	1.303 (0.78)	-0.379 (0.74)	<b>1.889</b> <b>(1.72)*</b>	1.300 (1.39)	0.646 (0.92)	0.801 (0.59)	<b>1.094</b> <b>(3.58)***</b>
NationalElection	0.695 (1.33)	-0.212 (0.89)	0.696 (1.33)	-0.214 (0.91)	0.692 (1.33)	-0.212 (0.90)	0.575 (1.18)	-0.232 (0.96)
EuropeanElection	0.157 (0.91)	<b>0.527</b> <b>(2.13)**</b>	0.163 (0.95)	<b>0.528</b> <b>(2.15)**</b>	0.158 (0.93)	<b>0.527</b> <b>(2.14)**</b>	0.076 (0.38)	<b>0.507</b> <b>(2.03)**</b>
REERt_1							-0.070 (1.30)	0.006 (0.46)
PrecrisisDeltaREER							-0.097 (0.83)	<b>-0.073</b> <b>(7.46)***</b>
_cons	<b>6.068</b> <b>(1.83)*</b>	8.213 (0.77)	<b>6.800</b> <b>(2.58)***</b>	<b>17.186</b> <b>(2.00)**</b>	<b>7.515</b> <b>(2.39)**</b>	<b>4.586</b> <b>(1.82)*</b>	3.414 (0.59)	<b>5.178</b> <b>(2.18)**</b>
N	418	307	418	307	418	307	418	307
Augmented Regression test	Passed	Failed (H-T shown)	Passed	Failed (H-T shown)	Passed	Failed (H-T shown)	Failed	Failed (H-T shown)

Pre-crisis construction share of GDP is statistically significant only in specification A3 (when private debt is not accounted for) and only for non-Euro Area countries. This might be explained, however, by the relation existing between construction and current accounts for monetary union countries (Adam et al., 2012). Similarly, private and public debt are statistically significant only for non-Euro Area countries, and only when included individually (specifications A2 and A3 respectively).

The coefficients for Banking Union and ECB's "whatever it takes" OMT programme behave as expected: they both are consistently statistically significant with a strong negative correlation to the crisis intensity indicator, suggesting that they both played a fundamental role in decreasing the risk premium on government bonds (which weights 50% in the indicator). Differently, the positive sign associated with the (statistically significant) coefficients of fiscal governance, financial aid leaves the door open to further interpretation. One way to evaluate the sign of  $\beta_{11}$  and  $\beta_{13}$  would be to consider a degree of reverse causation in the relationship between the crisis indicators and the respective variables. Fiscal integration was introduced at the very heights of the crisis, only very distressed countries received financial aid;

similarly, the collapse in GDP is associated with a fall in imports and labour costs, hence the negative coefficients of  $\beta_3$  and  $\beta_5$ .

On the one hand, this is expected by theory and in line with previous findings from Lane and Milesi-Ferretti (2013). In other words, the negative correlation between labour costs, current account and crisis index is simply a sign of the occurring adjustment, with the feedback effect on the crisis indicator happening with a longer lag than the one taken into account in this study. However, an alternative explanation may be that, indeed, austerity policies, embodied precisely by tightened fiscal policies and labour market reforms, all enacted through Memoranda of Understandings associated with bailout programmes, worsened, at least in the short term, the performance of the crisis indicator.<sup>14</sup> At first sight, this appears to be supported by the divergence in the sign of the coefficients for fiscal integration (negative for non-Euro Area countries, positive for EMU countries).<sup>15</sup> In other words, the sign of the coefficients is the one Austerity opponents (Tamborini, 2014; Stiglitz, 2015) expect to be. At this stage and with the methodology adopted in this paper, however, there is no sufficient information to determine whether we face a case of reverse causality, as it appears on first sight, or whether we are dealing with the real effect of the cited policies; nor was a final word on austerity the goal of the present work.<sup>16</sup>

The results of the comparative analysis seem to support the idea that, even if the origins of the crisis were widespread and not limited to Euro Area countries, Euro Area institutional setting played a role, being both associated with stronger adverse effects related with labour costs and current accounts' deterioration, and with lack of appropriate crisis-resolution mechanisms.

## 6.2. Pooled approach

---

<sup>14</sup> Both the International Labour Organization (2015) and the OECD (2012) have warned of the potential adverse effects of simultaneously enacting labour market reforms and considerable fiscal tightening.

<sup>15</sup> The sign of the coefficients for labour costs, however, remains unchanged, as well as the sign for bail out measures.

<sup>16</sup> One shall note, however, that –even if austerity policies might have had a worsening effect on the unemployment component of our indicator, they constituted the political condition for actions undertaken by the European Central Bank, which –as the model shows– has been fundamental in decreasing the intensity of the financial component of the crisis. Moreover, the current setting of the model does not take into account the continuous effect over time of policies associated with austerity; many of the policies enacted to reshape the competitiveness of distressed countries are hypothesized to yield results over the long run, and therefore their effect does not appear in the current setting of the model.

Six specifications were tested in the pooled database approach. Results are shown in table 3. The first specification (B1) takes into account both public and private debt, as well as all interaction terms of economic variables with pre-crisis Euro Area membership. Specification B2 drops the interaction terms for private debt accumulation, which would not make a difference between Euro and non-Euro Area countries. Model B3 excludes private debt variables, and related interaction terms (4 variables in total); B4 applies the same to private debt variables. Finally, Model B5 excludes labour costs variables substituting it with the REER index, and model B6 exchanges the incremental governance variables (both for fiscal integration and banking union) with a more detailed set of 6 dummy variables modelling the specific evolution of fiscal and banking governance,<sup>17</sup> to catch eventual individual effects, if any. Specifications B1-B3 and B6 passed with margins the *xtoverid* augmented test, while specifications B4 and B5 failed.<sup>18</sup>

Table 3- Approach B, Pooled

	B1	B2	B3	B4	B5	B6
construction_gdp	<b>0.566</b> (1.68)*	<b>0.758</b> (3.17)***	<b>0.506</b> (2.89)***	<b>0.739</b> (2.96)***	0.381 (0.96)	<b>0.566</b> (1.67)*
ExternalBalance	<b>-0.632</b> (4.02)***	<b>-0.479</b> (3.52)***	<b>-0.510</b> (3.89)***	<b>-0.559</b> (4.49)***	<b>-0.583</b> (4.28)***	<b>-0.628</b> (4.04)***
QuarterlyCurrentAccount	<b>0.165</b> (3.80)***	<b>0.165</b> (3.80)***	<b>0.164</b> (3.82)***	<b>0.164</b> (3.81)***	<b>0.164</b> (3.45)***	<b>0.165</b> (3.76)***
labourCosts_BUSINESS	<b>-3.720</b> (2.68)***	<b>-3.757</b> (2.75)***	<b>-3.779</b> (2.71)***	<b>-3.754</b> (2.76)***		<b>-3.648</b> (2.65)***
PrecrisisLabourCosts	<b>1.262</b> (1.87)*	<b>1.428</b> (2.21)**	<b>1.273</b> (2.09)**	<b>1.423</b> (2.20)**		<b>1.240</b> (1.85)*
PreCrisisPRIVATEdebt	-0.001 (0.05)	<b>-0.007</b> (1.87)*	-0.002 (0.30)		<b>-0.018</b> (2.37)**	-0.001 (0.06)
DELTAdebtPRIVATE	-0.051 (1.20)	<b>0.023</b> (2.11)**	-0.003 (0.16)		<b>-0.085</b> (1.91)*	-0.050 (1.20)
PreCrisisPUBLICdebt	<b>0.077</b> (3.13)***	0.042 (1.37)		<b>0.057</b> (1.79)*	<b>0.147</b> (5.92)***	<b>0.077</b> (3.15)***
DELTAdebtPUBLIC	<b>-0.097</b> (2.04)**	-0.013 (0.34)		-0.039 (1.06)	<b>-0.194</b> (3.20)***	<b>-0.097</b> (2.05)**
OMT	<b>-0.575</b> (2.74)***	<b>-0.575</b> (2.73)***	<b>-0.573</b> (2.74)***	<b>-0.575</b> (2.74)***	<b>-0.580</b> (2.83)***	<b>-0.401</b> (2.04)**
incrementalgovernance_fiscal	0.061 (0.89)	0.062 (0.91)	0.061 (0.90)	0.062 (0.91)	0.057 (0.72)	
incrementalBankingUnion	<b>-0.437</b> (4.26)***	<b>-0.439</b> (4.31)***	<b>-0.437</b> (4.30)***	<b>-0.439</b> (4.31)***	<b>-0.592</b> (3.94)***	
FinancialAidFirepower	<b>0.002</b> (2.60)***	<b>0.002</b> (2.62)***	<b>0.002</b> (2.62)***	<b>0.002</b> (2.62)***	<b>0.002</b> (2.32)**	<b>0.002</b> (2.71)***
NewMemberstate	<b>-2.735</b> (2.17)**	<b>-1.650</b> (1.80)*	<b>-1.756</b> (2.04)**	<b>-2.346</b> (2.94)***	<b>-3.171</b> (2.56)**	<b>-2.730</b> (2.17)**
Peripheral	0.879 (0.75)	-0.230 (0.29)	0.048 (0.08)	0.308 (0.45)	1.140 (1.25)	0.877 (0.75)
NationalElection	0.382 (1.22)	0.382 (1.22)	0.384 (1.22)	0.382 (1.22)	0.300 (1.02)	0.370 (1.18)
EuropeanElection	<b>0.320</b>	<b>0.319</b>	<b>0.321</b>	<b>0.319</b>	<b>0.316</b>	<b>0.468</b>

<sup>17</sup> The first step of the banking union, the common supervision mechanism, could not be modeled due to perfect collinearity with the Two-Pack, which was approved in the very same quarter as the banking supervision package.

<sup>18</sup> While B5's failure was expected, provided the same happened in the comparative approach, failure of B4 was unexpected, given that the comparable version of the comparative approach passed the test with a large *p* value.

	<b>(2.20)**</b>	<b>(2.19)**</b>	<b>(2.21)**</b>	<b>(2.20)**</b>	<b>(2.09)**</b>	<b>(2.92)***</b>
EURextPosition	<b>0.312</b>	0.183	0.120	<b>0.261</b>	0.082	<b>0.307</b>
	<b>(1.78)*</b>	(1.45)	(0.98)	<b>(1.84)*</b>	(0.77)	<b>(1.77)*</b>
EURPreCrisisLabourCosts	<b>2.660</b>	<b>2.857</b>	1.543	<b>3.646</b>		<b>2.633</b>
	<b>(1.78)*</b>	<b>(2.41)**</b>	(0.96)	<b>(2.53)**</b>		<b>(1.77)*</b>
EURdeltaPublicDebt	0.067	0.014		0.036	<b>0.146</b>	0.066
	(1.61)	(0.28)		(0.63)	<b>(3.06)***</b>	(1.59)
EURpublicDebt	<b>-0.066</b>	-0.023		-0.041	<b>-0.131</b>	<b>-0.066</b>
	<b>(2.11)**</b>	(0.83)		(1.51)	<b>(3.41)***</b>	<b>(2.11)**</b>
EURdeltaPrivateDebt	<b>0.069</b>		0.030		<b>0.113</b>	<b>0.068</b>
	<b>(1.83)*</b>		(1.41)		<b>(2.67)***</b>	<b>(1.84)*</b>
EURprivateDebt	-0.006		-0.006		<b>0.017</b>	-0.006
	(0.46)		(0.69)		<b>(1.70)*</b>	(0.45)
Euromembership	-0.922	-0.756	-0.845	-0.790	-1.097	-0.872
	(0.83)	(0.69)	(0.77)	(0.73)	(0.70)	(0.83)
REERt_1					0.041	
					(1.38)	
PrecrisisDeltaREER					<b>-0.048</b>	
					<b>(2.10)**</b>	
EuroREERt_1					<b>-0.145</b>	
					<b>(2.11)**</b>	
EURprecrisisDeltaREER					-0.053	
					(0.51)	
European_Semester						-0.104
						(0.48)
Two_Pack						-0.134
						(1.23)
TSGP						-0.187
						(0.86)
ESMentryintoforce						0.046
						(0.27)
EUBankAuthority						0.227
						(1.24)
BankingUnion_CR						<b>-0.859</b>
						<b>(5.17)***</b>
_cons	<b>6.204</b>	<b>4.578</b>	<b>8.130</b>	4.089	4.482	<b>6.072</b>
	<b>(2.00)**</b>	<b>(1.80)*</b>	<b>(4.50)***</b>	(1.51)	(1.10)	<b>(1.96)**</b>
N	725	725	725	725	725	725
Augmented regression test	Passed	Passed	Passed	Failed	Failed	Passed

The outcome in the aggregate approach features substantial differences from the results of the comparative approach. Notably, pooling data results in higher statistical significance of GDP construction share (across all specifications but B5) and the various public debt regressors. Specification B1 (when both public and private debt are taken into account) seems to suggest that both public and private debt accumulation before the crisis played a role, although -given the extremely small size of the coefficients- a secondary one. In particular, specification B1, B5 and B6 seem to suggest that private debt accumulation was a problem for the Euro Area in particular. Nevertheless, coefficients remain extremely small.

The small effect may in part be due to the presence of GDP construction share, which was fuelled by private indebtedness and whose effect is both large and statistically significant. Pre-crisis labour costs confirm the pattern already seen in the comparative approach, with large and statistically significant general coefficients, and even larger Euro-Area specific betas. Looking at integration measures undertaken during the crisis, fiscal governance fails to reach statistical significance in any of the analysed specifications, while banking union and the OMT programme replicates the results of the comparative model. In particular, a

Joint Wald Test in specification B1 on  $\beta_{16}EuroLabourCosts_{it} + \beta_{17}EuroPrecrisisLabourCosts_i + \beta_{18}EuroDeltaDebtPrivate_i + \beta_{19}EuroDeltaDebtPublic_i + \beta_{20}EuroPrecrisisDebtPrivate_i + \beta_{21}EuroPrecrisisDebtPublic_i$  leads to the rejection of the hypothesis that the coefficients all equal zero at 5% confidence level ( $\text{prob} > \chi^2 = 0.05$ ).

Overall, the results do not differ substantially from the comparative model, with two notable exceptions: first, the GDP construction share turns statistically significant when the databases are merged. Second, the comparative model suggested that pre-crisis external balance seemed about 30% more important in the Euro Area group, while the interaction coefficient between external balance and pre-crisis Euro Area membership seems to suggest the opposite in Specification B1.

One shall note, however, that this interaction term is seldom significant across specifications, and when so only at 10% level. Nevertheless, this constitutes the main divergence point between the two approaches.

The main results of the comparative approach -labour costs and current account deterioration before the crisis played a role, especially for Euro Area countries; debt accumulation did so in much lesser extent, and with unclear magnitude; the turning point in the crisis was the completion of the EMU architecture with a quasi-lender of last resort function for the ECB and a Banking Union- are substantially replicated in the merged approach, and seem to confirm the thesis that Euro Area membership had some responsibility (although very much shared with other factors) in the origins and duration of the crisis. Finally, the merged database approach is equally inconclusive when approaching the issue of the role played by austerity measures, i.e. whether the sign of the coefficients detects a degree of reversed causality or whether they indeed indicate an austerity-driven worsening of the crisis. As indicated previously, a final word on austerity policies is beyond the goal of this paper, which aims to detect whether Euro Zone membership, and in particular Euro Zone-induced, pre-crisis constraints, had a role in the crisis.

## 7. Robustness checks and Conclusions

A series of alternative models were tested on specification B1 to see whether substantial divergences would arise. Estimates for panel-robust OLS, panel-corrected OLS and Hausman-Taylor are reported in table 4,

along with the baseline Random Effects results. Fixed-Effects estimates are not reported because of the large number of time-invariant variables in the model. As shown in table 4, no substantial differences emerge; the sign, size and statistical relevance of the coefficients of interest is comparable across the four models; *DeltaPrivateDebt* reaches statistical significance only in the two OLS models, which also tend to estimate a stronger effect of all the Euro Area interaction variables. Finally, *OMT* fails to be statistically relevant in the panel-corrected version. With this single exception, the remaining variables of interest - *EURdeltaPrivateDebt*, *EURpreCrisisLabourCosts*, *avg\_externalBalance*, *avg\_constructionGDP* (which point in the direction of a partially endogenous explanation)- maintain sign, size and statistical significance across models.

Table 5- Robustness Checks (specification B1)

	Random Effects	OLS Panel-Robust	OLS Panel-Corrected	Hausman-Taylor
avg_construction_gdp	<b>0.566</b> (1.68)*	0.495 (1.51)	<b>0.495</b> (4.75)***	<b>0.560</b> (2.02)**
avg_ExternalBalance	<b>-0.632</b> (4.02)***	<b>-0.655</b> (4.66)***	<b>-0.655</b> (14.36)***	<b>-0.638</b> (5.79)***
QuarterlyCurrentAccount	<b>0.165</b> (3.80)***	<b>0.157</b> (3.75)***	<b>0.157</b> (10.53)***	<b>0.165</b> (11.64)***
labourCosts_BUSINESS	<b>-3.720</b> (2.68)***	<b>-2.590</b> (1.72)*	<b>-2.590</b> (5.53)***	<b>-3.756</b> (7.92)***
PrecrisisLabourCosts	<b>1.262</b> (1.87)*	0.730 (1.07)	<b>0.730</b> (3.37)***	<b>1.264</b> (3.70)***
PreCrisisPRIVATEdebt	-0.001 (0.05)	-0.003 (0.27)	-0.003 (0.74)	-0.001 (0.06)
DELTAdebtPRIVATE	-0.051 (1.20)	<b>-0.075</b> (1.73)*	<b>-0.075</b> (4.53)***	-0.053 (1.39)
PreCrisisPUBLICdebt	0.077 (3.13)***	<b>0.095</b> (3.57)***	<b>0.095</b> (7.28)***	0.077 (2.41)**
DELTAdebtPUBLIC	<b>-0.097</b> (2.04)**	<b>-0.132</b> (2.49)**	<b>-0.132</b> (6.02)***	<b>-0.099</b> (1.97)**
OMT	<b>-0.575</b> (2.74)***	<b>-0.584</b> (2.99)***	-0.584 (1.56)	<b>-0.573</b> (1.75)*
incrementalgovernance_fiscal	0.061 (0.89)	0.052 (0.71)	0.052 (0.37)	0.060 (0.49)
incrementalBankingUnion	<b>-0.437</b> (4.26)***	<b>-0.456</b> (4.41)***	<b>-0.456</b> (2.45)**	<b>-0.434</b> (2.65)***
FinancialAidFirepower	<b>0.002</b> (2.60)***	<b>0.002</b> (2.41)**	<b>0.002</b> (6.28)***	<b>0.002</b> (7.45)***
NewMemberstate	<b>-2.735</b> (2.17)**	<b>-3.332</b> (2.75)**	<b>-3.332</b> (6.63)***	<b>-2.779</b> (2.18)**
Peripheral	0.879 (0.75)	1.229 (0.99)	<b>1.229</b> (2.96)***	0.901 (0.82)
nationalelection	0.382 (1.22)	0.406 (1.19)	0.406 (1.46)	0.388 (1.59)
EuropeanElection	<b>0.320</b> (2.20)**	<b>0.311</b> (2.23)**	0.311 (1.09)	0.322 (1.29)
EURextPosition	<b>0.312</b> (1.78)*	<b>0.323</b> (1.83)*	<b>0.323</b> (5.54)***	<b>0.318</b> (2.13)**
EURPreCrisisLabourCosts	<b>2.660</b> (1.78)*	<b>3.101</b> (2.06)**	<b>3.101</b> (5.32)***	<b>2.691</b> (1.78)*

EURdeltaPublicDebt	0.067 (1.61)	<b>0.092</b> <b>(2.06)**</b>	<b>0.092</b> <b>(4.07)***</b>	0.068 (1.19)
EURpublicDebt	<b>-0.066</b> <b>(2.11)**</b>	<b>-0.083</b> <b>(2.57)**</b>	<b>-0.083</b> <b>(6.07)***</b>	<b>-0.066</b> <b>(1.91)*</b>
EURdeltaPrivateDebt	<b>0.069</b> <b>(1.83)*</b>	<b>0.088</b> <b>(2.22)**</b>	<b>0.088</b> <b>(6.03)***</b>	<b>0.070</b> <b>(2.04)**</b>
EURprivateDebt	-0.006 (0.46)	-0.001 (0.12)	-0.001 (0.34)	-0.005 (0.46)
Euromembership	-0.922 (0.83)	-1.893 (1.55)	<b>-1.893</b> <b>(3.79)***</b>	<b>-1.041</b> <b>(1.72)*</b>
_cons	<b>6.204</b> <b>(2.00)**</b>	<b>6.083</b> <b>(2.03)*</b>	<b>6.083</b> <b>(4.69)***</b>	<b>6.393</b> <b>(2.05)**</b>
N	725	725	725	725
R <sup>2</sup>		0.68	0.68	

Functional integration is, by definition, incomplete: it concerns only a limited amount of policies and institutions needed to address a particular set of problems. While generating benefits, it could create the conditions for new problems to arise. Did the pre-crisis integration, and the economic dynamics unleashed by the creation of the Single Currency, contribute to the Eurocrisis? The answer to this question is crucial for functionalist integration theory, which embodies a *crisis* > (incomplete) integration > *crisis* dynamics suggested by late functionalist theories like Schmitter (2002).

The paper attempted to answer the question against the testbed of the Eurocrisis by creating a composite index of the crisis itself and determining to what extent pre-crisis integration (or the lack thereof) are associated with its evolution.

In section 4 we discussed our working hypotheses. In the comparative approach, we expected to see relatively larger coefficients for the Euro Area countries, as well as seeing an effect of integration measures; in the pooled approach, we expected to have a series of statistically significant coefficients for the Euro Area interaction terms, and to see an impact of pre-crisis Economic performance in general. The results discussed in section 5 seem to confirm our working hypotheses in both models. Pre-crisis economic performance variables are, in average, 30% better predictors for Euro Area countries; the coefficient associated with pre-crisis performance on labour costs is particularly high in the Euro Area group, while failing to be statistically relevant in the non-Euro Area group. The pooled approach confirms this result, suggesting that precrisis private debt and labour costs increases were a relatively larger problem in the Euro Area than elsewhere. While the methodology adopted in this work and the ensuing results are of no help in

determining the effect of economic policies enacted during the crisis, they are sufficient to ground into a large panel of data the *integration>crisis* expected by functionalist theorists.



## Chapter Four: Spill-arounds, but mainly spillovers? A qualitative assessment of the crisis' functional outcomes

### Abstract

The European response to the crisis has generated a plethora of new policies, institutions and procedures. A consensus seems to exist that the theoretical model best fitted to describe the wave of crisis-led integration is liberal intergovernmentalism, given the importance of inter-governmental meetings in the management of the Eurocrisis. This paper aims to challenge this view: the first part of the paper provides an architectural analysis of crisis-led integration, showing that only a fraction of the new institutions and policies do fit into the intergovernmental scheme, while the majority do not. The second part of the paper focuses on the specific role of the European Commission, which has greatly evolved during the crisis. The role of the European Commission has always been stretched between two poles: on the one hand, the Commission was seen as "guardian of the Treaties", i.e. as the supranational enforcer of a multilaterally agreed, rule-based governance; on the other hand, the Commission is increasingly perceived as the "kingmaker" of the European political game, acting instead as the pivotal power in a supranational form of government. Against this background, one of the key neo-functionalist hypotheses is that, in times of crisis, supranational agencies will attempt to redefine and widen their autonomy in respect of their national masters, creating a dedicated, supranational political space. Through analysis of both legal acts and political discourse, the second part of the paper looks into Commission's role in shaping the discourse and the form of the new economic governance, with particular reference to the debate on the establishment of a contractual agreements' mechanism and on fiscal rules flexibility.

Note: a shortened version of this paper is in review at the Journal of European Integration.



# **Spill-arounds, but mainly spillovers? A qualitative assessment of the crisis functional outcomes**

## **1. Introduction**

The Eurocrisis has produced, and likely will continue to produce, a number of new institutions, policies, and projects to reform the Euro Area. Such a reaction to the Eurocrisis was, to some extent, expected and even anticipated: one of the leading approaches to European Integration, neo-functionalism and related theories, has always postulated that integration advances through crises. Nevertheless, whether the Eurocrisis-led integration is indeed a case of functional integration is still a very open question: there is a diffuse perception that the Eurocrisis has provided impetus for an intergovernmental overhaul of the EU: after all, the crisis resulted in three new intergovernmental treaties and one treaty amendment; in 41 European Council meetings from 2010 to 2015, in average one each 50 days; and in a strong mediatization of the role of national leaders, such as Mrs. Merkel. The prominence of intergovernmental politics during the Eurocrisis has been so high that few have attempted a neo-functional analysis of crisis-led integration (for instance Niemann and Ioannou 2015). Leading scholarship maintains that the prominently intergovernmental nature of crisis-led integration falsifies the neo-functional hypothesis. Against this background, this paper seeks to assess to what extent a comprehensive interpretation of the crisis is possible within the boundaries of an adapted neo-neo functionalist integration theory, by providing both a overall evaluation of the evolution of the EMU architecture, and in-depth analysis of two

cases of functional integration.

## 2. Theorizing crisis-led integration

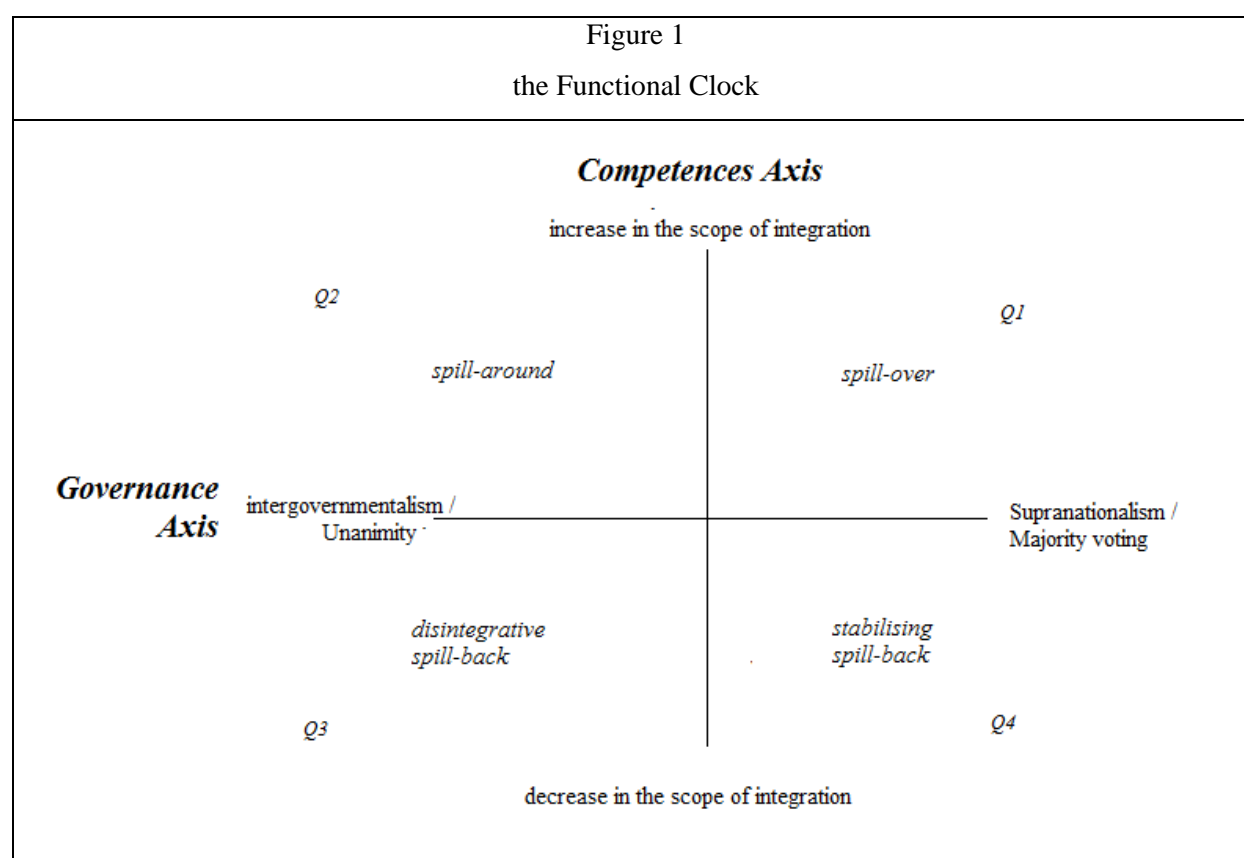
Haas (1958, 1964)) theorized that that supranational institutions could be able to extend their field of action and their autonomy over time, thanks in particular, to two processes: crisis-led integration and change in domestic preferences. In fact, incomplete integration in a given sector eventually leads to further integration/disintegration; either through “normal times”, non-disruptive incremental integration, or –in case of failure of incrementalism – through the outbreak of (largely endogenous) crises (Fabbrini, 2015). In classical Neofunctionalism either process would lead to the expansion of autonomy of the supranational institution (“spillover”). Also, as benefits of integration become evident, domestic coalitions are formed in order to push governments to attribute more competences to the institutions. Haas’ original theory, however, was not without limitations; in particular, it predicted a rapid expansion of supranational institutions, eventually towards a federal polity, that never happened (Haas 1975).

Many of the flaws of the original theory have been addressed by later functionalist scholarship, for instance by Schmitter (1969; 1970; 2002). In Schmitter (2002) setting, a particular crisis may induce 3 reactions: spill-over, spill-around, spill-back. Spill-over is defined as “the simultaneous increase in both level and scope of common institutions”; spill-around, instead, constitutes the creation of “specialized (..) but strictly inter-governmental institutions”; disintegrative spill-backs, finally, constitute the simultaneous reduction of both autonomy and scope of common institutions (Schmitter 2002, 32-33). These possible reactions to a crisis can be visualized as a set of possible variations on two axes: competences and governance (Figure 1).

The vertical axis reports an *increase/decrease* in the *scope* of integration (i.e. whether new functions are object of European decisions, or whether previously attributed functions are re-nationalised); the horizontal axis concerns the *increase/decrease* in the level of supranational decision making (i.e., whether the proposed reforms have a supranational or inter-governmental governance structure). In such a framework, for example, if a new policy attributes powers solely to the Commission would be qualified as a strong spillover; if the decision making process is co-decision, it would be closer to the origins, but still solidly in

the quadrant Q1; if the Council alone would take a decision, but acting by majority voting, this would constitute a very weak form of spill-around, very close to the intergovernmental system but using the one of the Union's legislative chambers; if the decision is in the hands of the Council or the European Council, or national parliaments under consensus rule, this would clearly fit in the spill-around Q2 quadrant.

As a consequence of the two-axes setting, a fourth option –labelled here as “stabilizing spill-back” – is reintroduced; such an option was present in Schmitter (1970) but largely neglected in following works. In fact, it is plausible that certain actors might develop a preference to decrease the scope of integration by removing certain competences, but simultaneously believe that the remaining Europeanized competences are to be dealt with in a more democratic/supranational approach (for example, by empowering the European Parliament); although this appears like a unlikely outcome and won't be discussed in this paper, once should notice that several “soft-Eurosceptic” parties ((Szczerbiak and Taggart, 2004) have developed precisely such position.



A second distinction from classical neo-functionalism is the importance attributed here to government preferences in this process. While the role of supranational policy-makers and civil society, the latter at national level as well, is not to be underestimated, when dealing with periods of intense crisis a particular attention to governments –which have the keys of Treaty reforms – is due (Fabbrini, 2015). Subnational preferences are, to some extent, considered as *given* by Governments when it comes to Treaty reforms; although the fundamental hypothesis of all strands of Functionalism, that preferences are endogenously constructed (see Chapter 1), still holds.

Finally, when completely divergent interpretations and solutions to a given crisis exist, agents may perceive that the costs of inaction are lower than the costs of both further integration and disintegration; for some time, therefore, no substantial integration is achieved despite a consensus exists over the dysfunctional nature of a given institutional setting. Typically, this is the case when actors agree on the limitations of the system but disagree on the solution, as in any “pseudo-trilemma” situation (see Chapter 2 for references). Over time, however, such costs erode the output-legitimacy of the supranational institutions (Scharpf, 1997; 2009) generating a rising popular opposition to integration (Hooghe and Marks, 2009; Scharpf, 2013). This may lead either to a re-alignment of national preferences, and therefore to integration, or to a spill-back outcome. The remainder of this section discusses the hypotheses behind spillover, spill-around, and disintegrative spill-back.

**Spillover:** the first set of hypotheses concerns spillover, i.e. the simultaneous expansion of both competences and autonomous governance of supranational institutions (quadrant Q1). While all kinds of spillover imply an increase in competences, we can distinguish two main types of spillover according with qualitative different governance settings: *insulation*, implying the increase of autonomus decision making powers of supranational executive bodies, and *parlamentarisation*, implying that new powers are managed through a classic Parliament-Executive dialectics, implemented at EU level through the Ordinary Legislative Procedure. First (H.1.1) if a given competence is already in the sphere of action of supranational institutions before the crisis, then a spillover outcome is likely. Second (H.1.2), if a competence is a “fundamental competence of nation states” (Bundesverfassungsgericht 2009: 252), and if risk-sharing or expenditure-sharing is

needed but a sense of shared identity exists, then a spillover outcome is likely; third (H. 1.3) if there is agreement on the need for (more) external monitoring/control (Majone 1998) of the given competence, then a spillover effect of insulation nature is likely. Finally (H.1.4) if the agencies are already insulated and have the power to re-interpret their mandate in autonomy, then a spillover effect is likely; this may include instances of “political spillover” related to electoral results of EP elections.

**Spill-around:** the second set of hypotheses concerns spill-around, i.e. the increase of competences in an intergovernmental framework (quadrant Q2). First (H.2.1) if a given competence is, ex ante, purely under control of national authorities or shared between the supranational and the national level, and no need for insulation emerges, then a spill-around outcome is likely: Governments, in fact, are assumed to (generally) prefer the minimum degree of integration required, and if it is possible to integrate a competence without losing decisional power, governments will attempt this solution. This also implies that a spill-around is more likely when the crisis is only weakly endogenous and due more to the lack of coordination rather than to a true malfunctioning of existing integration. Second (H.2.2) if a competence is a fundamental competence of nation states, or if risk-sharing or expenditure-sharing is needed, but there is no sense of common identity, then a spill-around is likely; third (H.2.3), if the costs of inaction are particularly large, i.e. there is a strong crisis dynamics leading the process of integration, then a spill-around is likely; finally (H.2.4), if the interpretation of the problem relies on failures of coordination, rather than on the need for insulation, then a spill-around is likely.

**Disintegrative spill-back:** the third set of hypotheses concerns the disintegrative spill-back, i.e. the reduction of both competences and autonomy of the supranational institution (quadrant Q3). First (H.3.1) if the crisis is attributed to the mismanagement of a given power/competence of the supranational level, then a spill-back is likely. Second (H.3.2), if the costs of dis-integration are perceived lower than the costs of both inaction and integration, then a spill-back is likely. Finally, if crisis-induced paralysis has completely eroded output legitimacy without a realignment of national preferences, then a disintegrative spill-back is likely.

By assumption, incomplete integration is in a condition of semi-permanent “functional disequilibrium” (Schmitter, 2002) which is likely to persist as long as the key competences of states are maintained at different level (Genshel and Jachtenfuchs, 2016); it follows that crisis-induced integration is likely to follow a dynamic evolution (H.4). The model presented above suggests that crisis-induced integration may follow a pattern of the kind *spill-over* > *spill-around* > *spill-over*. In a first phase, it is likely that existing institutions are amended in non-disruptive ways to deal with the new crisis; if this is insufficient, new competences are transferred to the Union, but in a rather intergovernmental setting; over time, the new policies and institutions will gain autonomy. Naturally, this paper does not aim to provide a comprehensive test for the many hypotheses of contemporary functionalism. The paper aims, however, to assess whether existing and forthcoming crisis-induced integration fits in the expectations informed by contemporary functionalism.

### 3. Eurocrisis-induced integration

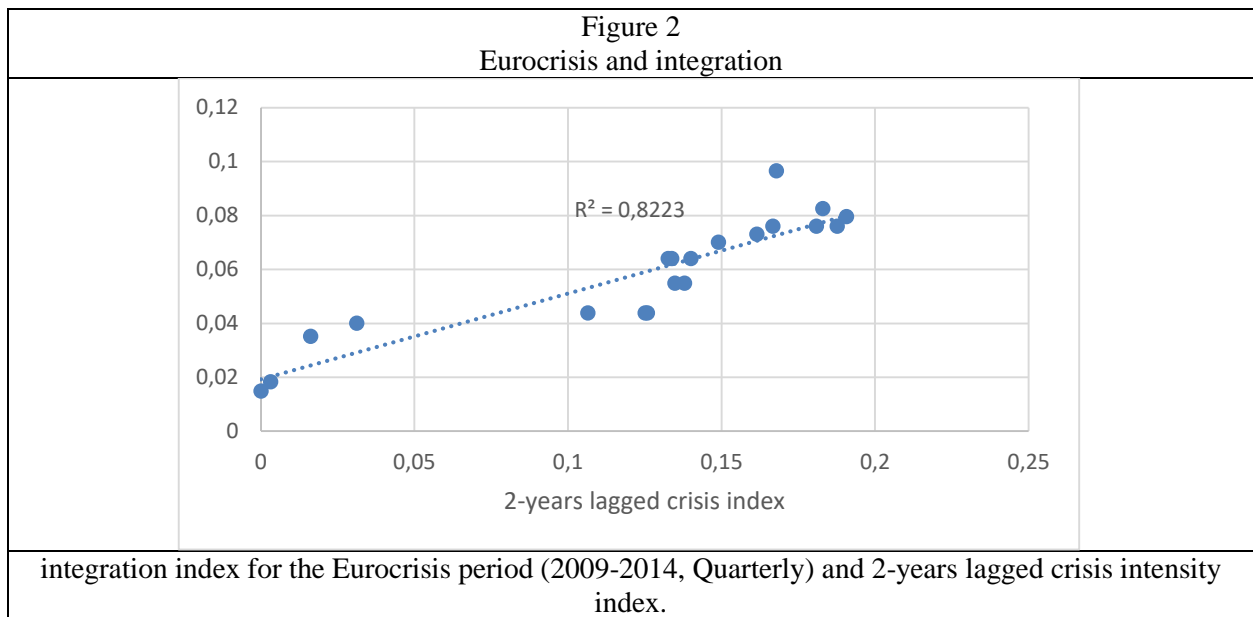
The Eurocrisis has surely pushed integration forward, corroborating the general underlying idea of all functionalist theories according to which “integration advances through crises” (discussed in Chapter 2). In particular, during the Eurocrisis institutional change has been particularly prolific (Figure 2): the connection between the index of European Integration developed by the ECB and the (2-years lagged<sup>1</sup>) index of crisis intensity developed in Chapter 3 is witnessed by a  $R^2$  above 0.8. However, this plethora of new institutions, policies and procedures are, likely, situated in different quadrants of figure 1.

While some have attempted a pure “neo-functional” analysis of the Eurocrisis (i.e., relying mostly upon the cases of “spillover”; see for instance Vilpikus 2013, Niemann and Ioannou 2015), a wider scholarship leans towards on the “mixed” nature of crisis-induced integration (for instance Fabbrini 2014, 2015; Dawson, 2014). In fact, the mixed nature of crisis-induced integration is an explicit feature of contemporary Neofunctionalism, both because, in times of crises, governments and supranational institutions have a role to play, and because of the dynamic nature of integration (as introduced in Hypothesis H.4).

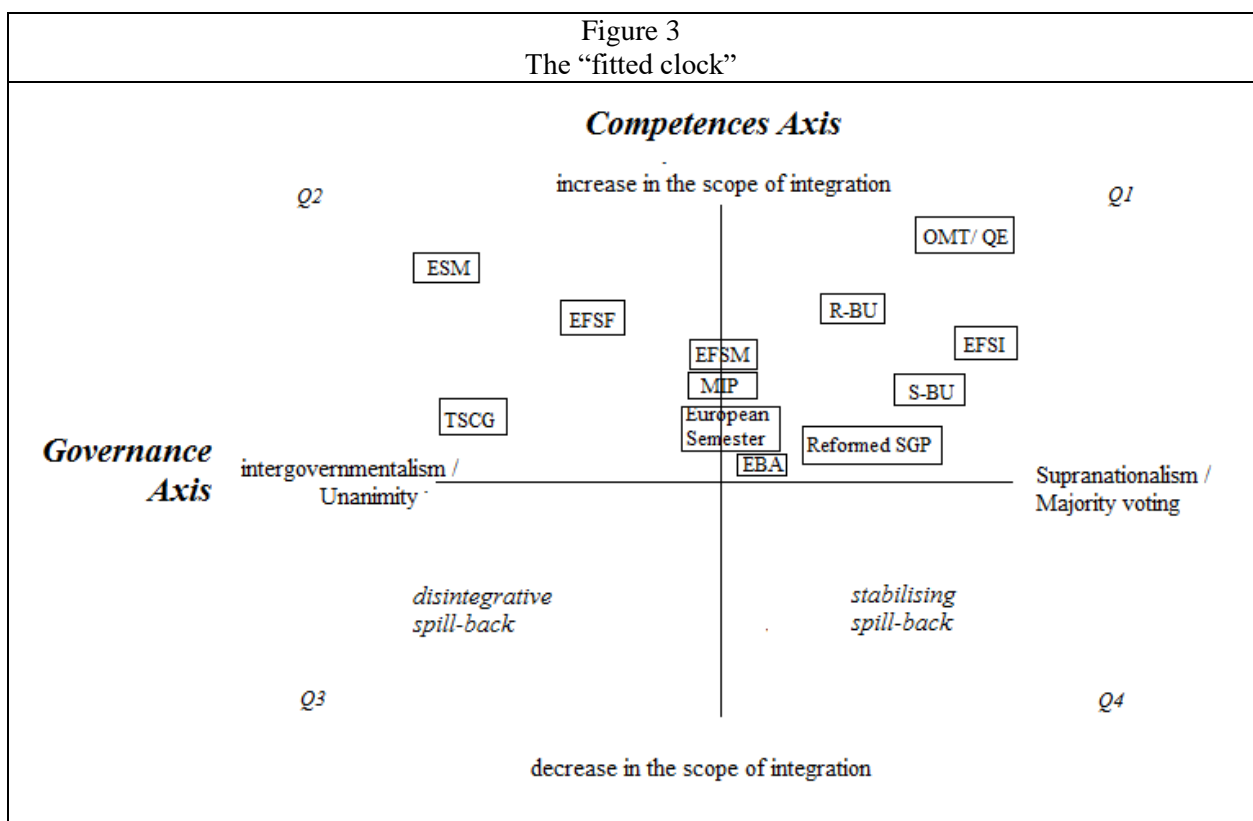
---

<sup>1</sup> The index is lagged two years, because I assume that a certain degree of crisis will set in motion the process of integration, which however takes years to bring up a policy change, which is then measured by the ECB index.





The goal of this section is therefore to understand which new policies and institutions fit in which quadrant of figure 1.



The following policies and institutions are considered: the reformed Stability and Growth Pact (SGP) ; the European Semester (ES, in its 2011 and 2013 versions); the European Financial Stabilization Mechanism

(EFSM); the European Stability Mechanism (ESM); the European Fund for Strategic Investment (EFSI); the Treaty on Stability, Coordination and Governance (TSCG); the Outright Monetary Transactions programme (OMT); the Supervisory pillar of the Banking Union (SBU) and the resolution pillar of the Banking Union (RBU). Figure 3 fits the “functional clock with all these institutions; the next two sections provide a discussion of each choice.

### *3.1 Instances of Spill-around*

The earliest case of spill-around is the creation of the EFSM in 2010 (regulation 407/2010). The Fund was set up in the wake of the 2008 global financial crisis and —differently from all other assistance funds set up during the crisis— it was grounded explicitly in the “solidarity” clause enshrined in article 122 of the TFEU. The regulation mirrors the mechanism established for non-Eurozone countries in 2002 to provide balance-of-payment assistance; the Commission becomes a borrower on behalf of the member-state, that so enjoys a very low interest rates thanks to the implicit guarantee provided by the EU budget. De facto, the EFSM provides an instrument for mutualization of domestic public expenditure, the maximal amount of “Eurobonds” so created is set to 60 Billion Euros.

In term of decision making process, the decision to whether granting an EU-backed credit line to a member-state is in the hands of the qualified majority of the Council. The EFSM constituted a first step towards the creation of Eurobonds and it is still part of the EU-anti crisis architecture; it paved the way for the much-larger anti-crisis funds such as the EFSF and ESM. Its governance system depends on the Commission and the Council’s qualified majority; this qualifies the EFSM as a hybrid institutional form, a very weak instance of spill-around. The creation of the EFSM would fit in H.2.1 and 2.2: although the provision of financial assistance in cases of circumstances “beyond [a member-state] control” was already a shared competence through art.122 TFEU, fiscal policy remains a fundamental competence of nation states, hence the sole decision making power (by majority voting) of the Council.

A second case of weak spill-around is constituted by the establishment of the European Semester of policy coordination in 2011 (amended regulation 1466/97) and its subsequent reform in 2013. The European Semester did not introduce, as such, new instruments, but it provided a much strengthened coordination of

existing tools. In respect to its predecessor, the Open Method of Coordination (OMC), the European Semester provided an expanded role for the European Commission, which acquired –through the Annual Growth Survey, an economic policy document published once a year—a stronger guidance role in addressing the general direction of the EU economy. Nevertheless the European Semester remains a fundamentally intergovernmental procedure: with the exception of the Annual Growth Survey (which holds no legal value) all acts coordinated through the European Semester are either originated in member-states, or need to be validated by a majority in the Council. The only relevant exception is the Excessive Deficit Procedure discussed in the next section, which is an integral part of the Semester. Overall, the establishment of the European Semester seems to fit in H.2.4, given that the need for better coordination, rather than for insulation, is the driver of this form integration. Nevertheless, further developments may occur (for instance, a stronger bond between the Parliament and the Commission on the Annual Growth Survey) which may push the Semester towards the quadrant Q1 (see Chapter 4).

Along with the European Semester, a third case of weak spill-around is constituted by the creation of the Macroeconomic Imbalances Procedure (MIP) in 2011. Grounded in articles 121 and 126 TFEU, the procedure allows the Commission to monitor the overall macroeconomic development of member-states and eventually propose sanctions against member-states failing to address their internal imbalances. The final decision on sanctioning is entitled to the majority of the Council, however. Moreover, as the decision is based upon a plurality of indicators (the Macroeconomic Imbalances Scoreboard), the violation of one single parameter is not sufficient to trigger the sanctions. This allows for larger flexibility in the hands of member-states when assessing the Commission's recommendations, making it easy for a coalition of states to turn down a request of sanctioning. Provided that economic policy is a competence of nation states and the treaty provides only for enhanced coordination of national policies, the creation of the MIP corroborates both H.2.4 and H.2.2.

A fourth case of (much stronger) spill-around is constituted by the follow-up funds to the ESFM: the EFSF and, subsequently, the ESM. The creation of the ESM, being a much larger rescue fund with a lending capacity up to 800 Billion Euros, could not be grounded in art. 122 (solidarity clause). Article 13, which prohibited central financing of national budgets, had to be amended in 2011 in order to allow for country

bailouts. A dedicated treaty setting up the new mechanism was signed in June 2012 and entered into force in October. The new institution is purely inter-governmental: there is no governing role for the Commission and all decisions are taken by representatives of the participating member-states.<sup>2</sup> The fundamental decision entitled to the ESM, namely to provide financial support, is to be taken by consensus of all participants (art. 5.6-ESM, detailed in art. 16.5-ESM). Further, several states have enacted national legislation for further ex-ante or ex-post authorization from their national parliaments, reinforcing –in the latter case – the intergovernmental logic of the instrument (Kreillinger 2015). Clearly, then ESM constitutes a case of spill-around fitting in h.2.2 and 2.3, given that the urgency of setting up a crisis mechanism was reiterated in several meetings of the European Council, but the creation of a fiscal instrument of this size clearly involved an intrusion in sovereign competences of nation states (Bundesverfassungsgericht, 2013).

### *3.2 Instances of Spill-over*

In some cases, crisis-led integration has resulted in a typical spillover effect, where both the competences of the supranational institutions and their autonomy are expanded. Besides the European Banking Authority, discussed below along with the banking Union, the earliest case of Eurocrisis-induced spillover is the 2011 reform of the Stability and Growth Pact, with particular reference to introduction of the reverse qualified majority principle. The 2011 introduction of reversed majority voting attributed substantial autonomy to the European Commission in (1) assessing whether countries are violating the adjustment requirements under the preventive arm of the SGP (art.6 and 10 regulation 1466/97) and (2) delivering sanctions under both the preventive (art.4 regulation 1173/2011) and the corrective arm (art. 5 and 6). The functional nature of the fiscal governance is discussed in detail in the next section of this paper.

A second instance of spillover is constituted by the ECB's reinterpretation of its own mandate through the well-known July 26<sup>th</sup>, 2012 “whatever it takes” speech by the ECB president Mario Draghi (Draghi, 2012a), the following setting up of the OMT programme (August 2<sup>nd</sup>, 2012) and the beginning of the Quantitative Easing in late 2014. The financial effects of the two announcements were sizeable (Altavilla, Giannone and

---

<sup>2</sup> It is worth noting that, in a recent case (*Ledra Advertising*, September 2016) the ECJ has recognised, for the first time, the role of the European Commission in the management of the ESM and of the following programmes, de facto bringing the ESM in the European legal sphere despite its original nature of separate international organization (Glinavos, 2016)

Lenza 2014) and considerably decreased the interest payment burden on several member-states. While in previous years the mandate of the ECB was perceived to be solely, or in the greatest part, to maintain price stability in the Eurozone, the ECB argued that for monetary policy to work smoothly, financial fragmentation is to be limited; financial fragmentation is due to the fear of collapse of the Euro, which translates in “exceptionally high risk premia hindering the effectiveness of monetary policy” (Draghi, 2012b). Therefore, as long as the countries are willing and ready to act domestically to reduce their risk premia, the ECB stands ready to protect the irreversibility of the Euro.

This reasoning, although still grounded in the fundamental ECB mandate of the ECB to conduct monetary policy of the Eurosystem (art. 282 TFEU) with the aim of maintaining price stability (art. 127 TFEU), extended this mandate to the preservation of the Eurosystem itself (without which no Eurosystem monetary policy is possible). This autonomous reinterpretation of the ECB mandate, which begun with the OMT but was extended with the Quantitative Easing policy fielded since late 2014, produced two side-effects; first, it induced the ECB to take a stance on non-monetary aspects of economic policy; second, it led to a substantial increase in the ECB’s public bond holdings, which may have redistributive implications (Sinn and W., 2012; De Grauwe and Ji, 2013; Bundesverfassungsgericht, 2015). Indeed, it is still unclear whether both the OMT programme and the Quantitative Easing programme are in accordance with the competences conferred upon the ECB; while a preliminary ruling favorable to the OMT has been released on January 14<sup>th</sup>, 2015 by the ECJ, a the final decision from the Bundesverfassungsgericht delivered in June 2016 maintains that certain conditions must be in place for the OMT programme to maintain its legality, thus opening the doors to future challenges from claimants. Despite the unclear legality of the OMT, it clearly constitutes a case of spillover corroborating both hypotheses H.1.1 and 1.4.

A third case of spillover is both the supervisory pillar of the Banking Union, established through the Single Supervisory Mechanism (SSM) in regulation 1024/2013, and the resolution pillar, established through the Single Resolution Mechanism (SRM) in regulation 806/2014. From a micro-functionalist point of view, the Spillover nature of the Banking Union is described in detail in Glöcker et al. (2016) through an historical-institutionalist perspective, which emphasizes the learning process and the role of non-state actors in

shaping policy evolution. However, a macro-functionalist perspective is missing from Glöcker et al. (2016), which fails to show why a Banking Union is to be considered a spillover rather than a spill-around.

The first pillar of the Banking Union confers upon the ECB the task of supervising systemic credit institutions at European level. Beforehand, supervision of the banking sector was held at national level but coordination was achieved through a series of three linked institutions agreed in 2010 and entered into force in 2011 (the European Banking Authority and the related Insurance and Securities Authorities). The Single Supervisory Mechanism, in other words, was created to address the shortcomings of existing crisis-induced institutions of intergovernmental nature. In particular, a full-fledged banking union, deemed as essential to address the crisis, was not possible without centralization of supervisory tasks.<sup>3</sup> The Supervision concerns approximately the 6000 largest banks in the Union, and becomes a second key competence of the ECB besides monetary policy; It's a clear case corroborating H.1.4 (need for insulation), as witnessed by recital 75 of regulation 1024/73.

The second pillar of the Banking Union, the SRM, is established in regulation 806/2014. The governing body is the Board of the SRM; it is composed by delegates of both the Commission and the Member states, but it enjoys full independence (art.47); it is accountable to the Commission and the Parliament; most decisions are taken by simple majority (art.52.1). Although the entrance into force of the Single Resolution Fund managed by the SRM is linked to the ratification of an international treaty, the Agreement on the Transfer and Mutualisation of Contributions to the Single Resolution Fund ("the Agreement"), once the ratification process is completed the Board acquires independent powers on the budget. As witnessed by recitals 2-4, 9 and 10 of regulation 806/2014, the rationale for the SRM is achieving better insulation and coordination, fitting therefore in H.1.3. On the other hand, the SRM is a clear case of risk-sharing mechanism; as no common identity exists, we would expect a spill-around rather than a spillover (H.1.2/2.3). However, the SRM is a *sui-generis* example of risk sharing: the public power is exonerated from contributing in the Single Resolution Fund, which is completely set up by contributions of the banking sector; as the public power is not involved, the lack of common identity does not constitute a limitation to

---

<sup>3</sup> See consideranda 9-12 of regulation 1024/2013.

the creation of mutualization instruments (see Chapter 5 for a more in-depth analysis of the connection between identity and redistribution).

Finally, a fourth case of spillover is constituted by the creation of the EFSI, also known as “Juncker Fund”, also discussed in detail in the next part. Although the Fund relies on a mix of financial contributions from the member-states delivered on a voluntary basis and of a smaller amount of resources drawn from the EU budget, both the inception of the Fund and its structure are of clear functional origins. The Fund was promised by the candidate Jean Claude Juncker during its campaign to win the European Elections and secure, for the first time, a political nomination to the European Commission Presidency; in other words, it is an eminent case of “political spillover”: as Commission presidential candidates are, following the amended article 17.7 procedure, elected by the European Parliament, political commitments to expand the reach of the Union within the existing mandate become possible. In term of governance, the Fund fits clearly in the spillover category: the Steering Board – composed for 75% by Commission officials and for 25% by EIB officials—is in charge of its management Moreover, despite the voluntary contributions from the member-states, Article 7.4 of the Regulation ensures full insulation from national political agendas, *de facto* excluding member states from the management of the investment fund.

Overall, the analysis carried out in this section has shown that the intergovernmental nature of crisis-led integration has probably been overestimated. Of all episodes of integration occurred in the wake of the Eurocrisis, five are typical spillover effects with a prominent role for insulated, supranational institutions: the two pillars of the Banking Union, the reform of the SGP, the EFSI, the OMT/QE of the ECB. Three procedures are a very weak form of spill-around, where governments are the ultimate decision-makers through their ministers in the Council, but only in dialogue with the Commission itself and through majority voting: this is the case of the ESFM, the MIP, and the European Semester in general. The only clear cases of strong spill-arounds are the EFSF/ESM and the TSCG. While governments have surely played a fundamental and extremely apparent role in the decision making process that led to the creation of many those institutions (with the relevant exception of the OMT, of the EFSI, and of the reformed fiscal rules) the institutions and procedures themselves lean towards supranationalism more than usually described; nor could governments play a smaller role in the decision making process, provided that most of the policies

object of integration during the crisis were of clear national competence still in 2010, thus requiring further transfers of competences through intergovernmentalism (Fabbrini 2015) to avoid cases of “ultra vires” violations of the EU mandate (Bundesverfassungsgericht, 2013).

#### **4. The Fiscal Rules Epos as a case of spillover?**

The reform of the SGP, occurred originally in 2011, has been only hinted in the previous section. In fact, the European framework of fiscal rules goes far beyond the SGP, encompassing laws, procedural norms, and political bargain. This section of the paper discusses the fiscal rules evolution during the crisis in detail.

The original set of fiscal rules of the EU, laid down in articles 121 and 128 of the now-TFEU and operationalised by a protocol known as the Stability and Growth Pact (SGP) was established in 1997 and reformed several times thereafter. It was originally organized on two well-known pillars (the “preventive” and “corrective” arms) with three goals: preventing excessive deficits, ensuring debt convergence, and ensuring medium-term deficit reduction. Their reform, however, is a key element of divide among member states since their inception.

##### *4.1 the EMU fiscal rules*

With the political agreement reached with the Treaty of Maastricht, the fiscal pillar of the EMU was characterized by a dual nature: on the one hand, it had to be enshrined into clear and justiciable rules; Germany, in particular, sought such a system to prevent to become “the paymaster of the EMU” (Fabbrini, 2015: 23). France, on the other hand, prioritized the maintenance of formal domestic competence on fiscal and economic policies. The resulting fiscal institutions created binding rules whose application, however, was decided upon by the member-states themselves. The full extent of this early, intergovernmental politicization of the Stability and Growth Pact (SGP) fiscal rules appeared in 2003, when the Council down-voted a Commission proposal to begin an excessive deficit procedure against France and Germany; the rules themselves were reformed two years later to codify the intergovernmental nature of the decision making process on fiscal policy. The 2005 reform was explicitly introduced in order to grant larger autonomy to governments and weaken the Commission’s power of delivering sanctions. Between the 2003 attempt and 2011, the role of the Commission was limited to monitoring the Member States’ behavior and



eventually enact the decisions of the Member States. In other words, during the first 10 years of the EMU (and in absence of any substantial crisis) the neo-functionalist assumption that agencies would have managed to increase their autonomy appeared to be definitively buried. The Eurocrisis, and in particular the scandal ensuing the Greek mis-reporting of deficit figures, changed the member-states perception on fiscal rules and provided space for the Commission to act. The SGP was modified again, this time in the opposite direction, in 2011, tightening the thresholds for Euro Area member states and introducing the Reversed Majority Voting principle on sanctions.

In the new setting introduced in 2011, the Commission acquired a large autonomy vis-à-vis the member states. The Commission is granted the automatic approval of decisions on sanctions unless member states in the Council succeeds in crafting an opposing majority; this corresponds to Neofunctionalist expectations on widening of autonomy of supranational agencies. However, its freedom of action in deciding which Member States were to be subject to the procedures was largely constrained by the tightening of the parameters themselves; political discretionality failed to appear in this first overhaul of the fiscal rules. In other words, between 2011 and 2015 the Commission acted (concerning fiscal rules) more like an “insulated” supranational agency (Majone, 1998) than like an executive enforcer with freedom of action. As such, this result corroborates only in part the neo-neo functionalist account of crisis-led integration, because only regulative autonomy succeeded to emerge at that stage. The SGP reform was accompanied by four other important measures in fiscal policy: the introduction (with the Six Pack) and reform (with the Two Pack) of fiscal monitoring and coordination; the introduction (with the Six Pack) of a common fiscal framework; and the approval of the Treaty on Stability, Coordination and Governance (TSCG-also known as Fiscal Compact) which requires the constitutionalisation in national basic laws of the fiscal rules introduced with the 2011 SGP reform. In sum, the period 2010-2013 has been characterized by intense reforms in the fiscal and economic framework of the Union, pointing towards the direction of more supervision, more control, and more sanctioning <sup>4</sup>.

#### *4.2 from fiscal rules to broader governance*

---

<sup>4</sup> Regulations 1173/2011, 1174/2011, 1175/2011, 1176/2011, 1177/2011 (“Six Pack”), 472/2013, 473/2013 (“Two Pack”)

In terms of institutional innovation, and in spite of the growing political rejection of austerity policy, the fiscal rules issue was settled in 2011/2012; it would remain settled for the remaining duration of the Barroso Commission and would not be reopened until the election of the Juncker's Commission. However, in other fields, the evolution of the economic governance did not halt; in fact, since 2012 the EU has entered in a phase of long-term overhaul of its governance setting, grounded in the partially-accomplished 2012 Four President Report, and in the rather new 2015 Five Presidents Report. A key element of the broad EMU governance is the European Semester. The European Semester of Policy Coordination lays at crossroads of the reformed governance, and yet it is perceived as the weak juncture of the overall architecture. Introduced informally by an Ecfm agreement in 2010 and codified in legislation by December 2011, the European Semester inherited the practice of economic policy coordination applied in Europe since the Maastricht Treaty, in particular the "Broad Economic Policy Guidelines" and the "employment guidelines" (the main building blocks of the so-called "open method of coordination[OMC]" introduced to achieve the goals of the Lisbon 2010 Agenda- Deroose et al., 2008), the "national reform programmes" that member states had to deliver as a part of the OMC, and the "stability plans" delivered according with the SGP.

The 2011 reform integrated the guidelines into a single document of economic policy, the Annual Growth Survey (AGS) approved by the European Commission in October each year. By April, Member states have to submit their Stability Plans and National Reform Programmes presenting their actions to implement the AGS goals and the fulfillment of SGP obligations; by June each year, the Commission and the Council deliver a set of recommendations to member states concerning the yearly priorities about their budgets and economic policy. In March 2013 the process was strengthened even further by adding a supervision of the actual implementation in national budget plans of the commitments undertaken in the programmes submitted in April: by end of October member states must submit their draft budgetary laws for the following year, and the Commission is in charge of checking their compatibility with recommendations delivered previously in the year. Nevertheless, the Semester remains burdensome but ineffective (Juncker, 2014). There are currently no means to induce a country to respect its own commitments; only the subset of recommendations concerning deficit and debt reduction can be enforced through the preventive and corrective arms of the SGP. The existence of macroeconomic imbalances could also be potentially sanctioned under the new Macroeconomic Imbalances Procedure introduced in 2011, but it has never been

used so far and moreover its criteria do not constitute, *di per se*, a set of policies or economic measures. As a consequence, the EU is missing an instrument to deliver any incentives (both negative, like sanctions, and positive, like financial support) to implement the country-specific recommendations.

To address this issue, a proposal for establishing a system of contractual agreements circulated since early 2011, and became one of the flagship initiatives of the late Barroso Commission to reform the Economic Governance. The fundamental idea of a contractual agreement mechanism is to achieve convergence and coordination through financial incentives. Of course, the idea, as such, is not new: it constitutes the backbone of international aid schemes such as IMF or World Bank programmes, and, of late, of the ESM. However, the main flaw of existing bailout-for-reforms institutions is that they tend to intervene with a little-negotiable top-down approach which entails important losses of sovereignty, and often they do it so late that the reforms needed to address the structural bottlenecks of the sick economies often have disruptive social and political costs. As a consequence, national elites prefer to avoid or eventually delay IMF or ESM intervention, further aggravating the economic situation and the expected social costs of lending institutions' intervention. Instead, convergence has to happen before, preventing a crisis from arising, when comparatively smaller effort is needed and thus conditionality could be less strict, strengthening ownership.

The creation of such a system of contractual agreements has been discussed, under various labels, in each Head of States and Governments' meeting since June 2012. It constituted the key priority of the Van Rompuy report endorsed by the European Council in December 2012. A first proposal from the Commission (Communication 165/2013) was put forward in March 2013. Later in the year, the Contractual Agreements' mechanism became one of the cornerstones of the Franco-German bilateral agreement of May 21st, 2013. It was further discussed in the European Council meetings of June, October and December 2013. The last European Council of 2013 registered, for the first time, a preliminary agreement on the forms, functions and structure of the "partnerships for growth, jobs and competitiveness"- the final denomination of the contractual agreements' mechanism in the EU jargon.

In fact, the analysis of the Council's conclusions since 2012 shows that, although member-states agreed, in principle, on the need of having an instrument to support the implementation of structural reforms, a deep disagreement existed on what had to come first: whether the binding element inherent in the contractual

approach, or the solidarity element inherent in the joint financing. Although the Council's conclusions do not formally report which countries supported which positions, one could bet safely that peripheral member states belong to the second group while core member-states to the first. While in the 2012 Van Rompuy report and in March 2013 Commission's Communication solidarity and binding partnerships were part of the very same instrument, since the December 2013 Council the proposal was split into two components: the (binding) partnerships for growth and jobs (upon which a wide consensus existed) and the connected "solidarity instrument" at its support, for which no consensus was reached. For peripheral countries, however, it was out of question to accept binding recommendations without funding; and it is no coincidence that the proposal disappeared from the Council agenda during the Italian Presidency, whose Parliament voted, back in March 2014, a political motion which considered as "not advisable" the establishment of contractual agreements (Mozione di Controllo, Friday 7th, March 2014). Similarly, the President of the European Parliament Mr. Schulz (a heavyweight of the European Socialist Party, much like Renzi) expressed in February 2015 his opposition to the proposal – defined as a "Frankenstein Construction"—in front of the European Council (Schulz, 2015).

#### *4.3 EFSI as a back-door for fiscal rules flexibility*

The failure of the contractual agreements' proposal constituted a setback in the strengthening of the economic governance, given that a large share of member-states favored the idea, which constituted one of the flagship initiatives of the late Barroso Commission. The Italian Presidency had, in fact, its own agenda for the reform of the Governance, with the intention to forge a coalition of governments to re-open the fiscal rules issue. Since 2014 there had been a growing pressure (especially coming from the French and Italian governments (Economist, 2015), but also from the International Monetary Fund (Akitoby et al., 2013)) to introduce "flexibility" into the European system of fiscal rules. A fundamental element of disagreement between member states, however, stems from the divergent understanding of what *flexibility* in fact means: rule-based flexibility for certain member-states, and political flexibility for others. The first approach, rule-based flexibility, has been inspired by supranational institutions like the IMF. Its goal is to design more sophisticated rules aiming to model large numbers of potential "states of the world" and thus prescribe behavior in each of the different possible scenarios. In fact, while before the crisis it was widely recognized

that fiscal rules should have been general enough to ensure broad understanding and public oversight (Kopits and Symanky, 1998) the crisis has produced a system of increasingly sophisticated rules which are deemed to increase flexibility by allowing differentiated adjustment to differentiated shocks (Akitoby et al, 2013; Eyraud and Wu, 2015). Under this approach, the rule allows for more (or less) fiscal margin in each of the hypothetical situation modeled in the rule, with complexity (and thus, lack of public oversight) increasing thereafter.

The alternative approach relies on political flexibility (and, as a matter of fact, had been in force between 2005 and 2011): the creation of a rule as simple as possible, with as little sanctioning as possible, to leave extensive margins for national decision making in the hands of national politicians. This second approach has three main advantages: it maintains simplicity and public oversight; it maintains national decision-making avoiding “one-size-fits-all” policies; and it is not intrusive for national sovereignty but in the most excessive cases. This approach relies, rather than on regulation and sanctioning, on monitoring, oversight, peer pressure and ultimately on trust, and enjoyed its golden moment the period between the 2005 and 2011 SGP reforms. However, it suffers from one key disadvantage: it relies excessively on member-states’ goodwill, which –as shown by the failures of the fiscal framework in the 2005-2010 period— could be easily abused.

The first solution (rule-based flexibility) is opposed by southern member states, which struggle to explain to the electorate the existing fiscal rules. Those governments instead emphasize the need for strengthened trust and solidarity (Italian Government, 2015) and a wider interpretation of rules to allow for less austere fiscal policies (Spiegel et al, 2014). The second solution (political flexibility) is unthinkable for northern member states, because it would provide a wrong set of incentives to member states for overspending and losses’ mutualisation, as witnessed by the Bundesbank Chairmann Mr. Weidmann (2012), and by the German Chancellor Mrs. Merkel and her Finance Minister in 2014. Indeed, the perception appears to be that softening of the rule-based control on fiscal policy would reproduce a moral-hazard situation not dissimilar from the first 10 years of the EMU, when the collapse in the 10-years interest rates in public bonds removed the market-based incentive to fiscal sustainability and rules were not strong enough to ensure compliance (Sinn and Wollmerhausen, 2011; Sinn, 2014).

The overhaul of economic governance was one of the priorities of the newly elected Commission President, Mr. Juncker. In fact, as recalled by the Italian Prime Minister in 2016, the reform of fiscal rules constituted a fundamental element of the political agreement between PES and EPP that led to the election of Juncker (Jones 2016). Juncker's Commission was supposed to be a "political Commission" since its very inception, as Juncker himself recalled in the discourse given in front of the European Parliament plenary on July 15th, 2014, just before the vote that would have seen him elected Commission President. In practice, however, Juncker was able to leverage on member-states divisions on these fundamental understanding of fiscal rules; the apparently unbreakable impasse between member-states was addressed by granting more decisional power to the Commission, which translated in larger political autonomy from member-states governments.

Moreover, the failure of the contractual agreements' proposal, largely by Italian hand, had left the door open to other mechanisms of financing domestic policies with pooled resources which had not to go through the burdensome European Semester process; the precision of recommendations delivered as a part of the Semester left little space of action both to the recipient member-states and to the Commission itself, which can only propose recommendations. Juncker's strategy built, therefore, on two pillars: on the one hand, on the contrasts between member-states concerning fiscal rules; on the other hand, on the need for some form of financing that peripheral member-states craved. On these bases, Juncker managed to forge a political agreement between the EPP and the PES in the Parliament which secured his election against the will of several member-states, and had himself claiming later of being the "first President of the Commission elected by the European Parliament" (Juncker 2015b, 2016). The flexibility clause and the EFSI are the result of this attempt to break the impasse on the governance reform, and through both policies –which are to be interpreted together – the autonomy of the Commission was substantially strengthened.

With regard to the particular debate on fiscal rules, Juncker undertook a series acts focused on finding a compromise between the two divergent visions; the implication of the compromise that Juncker was able to forge, however, was simultaneous strengthening the role of the Commission as executive entity. Two acts, in particular, are relevant: the so-called 'flexibility clause', enshrined in Communication 12/2015, and the 'golden-rule' included in the regulation on the newly-minted European Investment Fund.

The two acts are, in fact, to be considered jointly: the flexibility clause, introduced in February in the Stability and Growth Pact, provides two fundamental elements of freedom to member states. First, member states can ease their fiscal adjustment pattern towards the Medium Term Objective (MTO) as long as the concerned member state is coordinating its structural reforms' effort with the European Commission (COM 12/2015: 9-14). This is no trivial issue, because the definition of 'structural reform' is left open in the Communication. Although criteria for eligible reforms are set (the reform must be 'major', with 'long-term positive budgetary effects', and must be 'fully implemented' - *ibid.*:10), several minor reforms may be aggregated in 'well-designed comprehensive packages of reforms (...) which reinforce each other's impact through an appropriate choice of policy mix and sequencing of implementation' (*ibid.*: 10). The assessment of all these conditions is left to the sole judgment of the European Commission. The same applies to the 'long-term positive budgetary effects' clause, whereby it is stated that reforms boosting potential output may be included in the list. At the end, the Communication 12 provides such a large interpretation of the flexibility rule that, *de facto*, the rule is emptied of its cogent power and the decision is transferred from a rule-based governance framework into a politically-brokered government setting, where the Commission, and not the member-state, is the king-maker. This constitutes a departure from both the wishes of core member-states which were looking for a stronger set of rules and from those of peripheral member-states, which were looking for a repatriation of decision-making power on fiscal issues.

Second, a similar reasoning is applied to the second element of the flexibility clause, the coordination of investment effort within the Juncker Investment Fund. The political dynamics, here, is even more pronounced. Communication 12/2015 and Regulation 1017/2015 are to be considered jointly. The Communication states that both initial financing to the Fund (COM 12/2015:6) and contributions to the co-financing of the projects (*ibid.*: 8) will not be considered in computing deficit and debt threshold for what concerns the SGP requirements, although it must be noted that co-financing is subject to further clauses concerning the effect on the final position of the country. Investing through the Fund, in sum, provides member-states with a "golden rule" for which investment is not computed as deficit for the application of the fiscal rule. However, there is no automaticity between Fund's contributions and disbursements. The managing of the Fund is left to the Steering Board, composed for 75% by EC officials and for 25% by EIB officials. Article 7.4 of the Regulation states that:

‘Neither Member States nor other third parties shall be granted membership of the Steering Board, nor shall they be granted a role in the appointment of other EFSI staff including members of the Investment Committee, nor shall they have any right concerning other aspects of governance of the EFSI.’ (Regulation 1017/2015, art. 7 comma 4)

De facto excluding member states from the management of the investment fund. The combined effect of the Regulation and of the Communication can be summarized as follows: member-states are freed from binding fiscal rules for what concerns investment decisions and current expenditure, provided they surrender sovereignty to the Commission (and the Commission only) on investment decisions. Through the combined effect of the regulation, president Juncker appears as offering a bargain to the member-states: the opportunity to increase their current expenditure as much as they surrender investment decisions to the Commission. By considering jointly the flexibility clause and the golden rule, the new role of the Commission emerges clearly: not any longer a mere enforcer of fiscal rules, but a true player in the field of fiscal policy. Moreover, by taking on for the Commission the political authority of deciding on flexibility, Mr. Juncker aims to remove (at least formally) the northern-European lack of trust on southern political elites. Europe is thus heading back to “fiscal government”, but where the key decision-maker is in Brussels and not in Rome (or Paris).

Moreover, the flexibility clause, as envisaged by the Commission, constitutes a “coming back” through the backdoor of the logic behind the Contractual Agreements’ proposal, which disappeared from any official European document since October 2014. De facto, “flexibility in exchange of reforms” is exactly the logic of a contractual agreement as proposed by Bonatti (2014) memo to the Italian Presidency of the Council of the European Union. Moreover, the commitment of Juncker to adapt, in the incoming 2016 review of the Multiannual Financial Framework, the use of the existing Funds to address specific parts of the Country-Specific Recommendations constitute, as well, a step towards the implementation of the agreements. The Commission, however, takes for itself –and not for the European Council or the Eurogroup, as envisaged in the original proposal – the right of deciding which countries, under which conditions, shall receive the flexibility space. This might not take the form of a formal, legally binding contract but has shown at least in one occasion its practical functioning: in October 2015 the Commission has signaled it is willing to grant



a flexibility exception to the 3% SGP target for certified expenditure occurred in the framework of migration assistance (Juncker, 2015).<sup>5</sup> Under the contractual agreements' scheme, which targeted specifically competitiveness' enhancing reforms, this would not have been possible, as only a specific list of actions were to be included in the framework, thus constituting an additional form of politicization of the governance enacted by this Commission.

In sum, the Juncker Commission has strengthened its hand in economic matters. It now disposes of the instruments to deliver sanctions not only on fiscal issues but also on macroeconomic matters; it can decide, formally in autonomy, upon the nature and the extent of the flexibility clauses to be applied to member-states, and what member-states have to do in order to profit of such clauses; and finally, together with the EIB, it represents the master of the new Fund for Strategic Investments through which member-states have to pool capital investment if they want to acquire further budgetary flexibility for current expenditure. In other words, the Commission has now larger discretionary powers on fiscal rules and related policies than ever before; it has therefore acquired, in the domain of economic governance, an unprecedented political autonomy.

#### *4.4 stronger powers, stronger legitimacy?*

A key question ensues from this progressive politicization and substantial strengthening of the Commission competences: does the Commission ("the unelected bureaucrats") have sufficient legitimacy to take such decisions in a field of traditionally strict democratic competence) On the one hand, today's Commission enjoys a democratic legitimacy unknown to previous officers. On the other hand, the Commission has acquired, formally and informally, powers and competences it was not originally conceived to hold.

In term of overall democratic legitimacy of the Commission, the change introduced through the article 17.7 TEU in the Treaty of Lisbon are of sure relevance. The electoral link between this Commission and its Parliamentary Majority. Mr. Juncker, being the first President elected through the new procedure and having competed in open elections against Martin Schulz, can rightfully claim a degree of direct democratic

---

<sup>5</sup> It is worth noting that the only country requiring in its own draft budget delivered by October 15<sup>th</sup> was Italy, for an amount of 3.2 Bn (roughly 0.2% of the Italian GDP).

legitimacy which was unknown to his predecessors. Moreover, the Parliament has been able to impose its candidate to the European Council despite an early veto from Merkel and a final “no” from Cameron. The process has brought about a strong political coordination between the “great coalition” and the President of the Commission. While the existence of a Great Coalition in the European Parliament is not new, the polarization of the Parliament has increased thanks to the growing success of Eurosceptic parties, which control- both in the soft ECR groups and in the extreme EFD and ENF- around 20% of the Chamber. The other oppositions in the Parliaments- the Greens and the Left- control another 15% more, so about 35% of the Parliament systematically vote against the ruling coalition, an unprecedented polarization for the Hemicycle. This has led to constant meetings between the President of the Commission and the leaders of the ruling parties, which have been reported to meet once or twice per month (Palmeri 2015) to coordinate the actions of the parliamentary majority and the Commission itself. Nevertheless, this unprecedented formal and informal bond between the majority of the Parliament and the European Commission is of little effectiveness outside of the areas of competence of the European Parliament: the role of the latter in fiscal and economic policy-making at EU level is still negligible. In fact, none of the reforms of the economic governance occurred since late 2010 has strengthened the Parliament considerably. Economic and Monetary Dialogues are not more than formal hearings of the Commission and of the Central Bank in front of the Parliament, but fail to attribute any legislative or sanctionatory power to the European Parliament. For the large part of secondary legislation approved since 2010, this choice is in line with the fundamental inspiration behind the Lisbon Treaty according to which economic decision making is to remain a core competence of member states, and the involvement of the Union’s institutions is only required for a. structuring coordination and b. enforcing intergovernmentally-agreed rules. The shift from governance to government of fiscal rules was not expected nor, indeed, accounted for in the Treaty of Lisbon.<sup>6</sup>

## 5. Conclusions

---

<sup>6</sup> Less reasonable, however, is the lack of formal involvement of the Parliament in procedures which have been designed ex-novo during the crisis by means of new treaties: the ESM and the TSGP in particular. However, both new treaties have been signed by the national governments as measures intended not to endow the Union with permanent institutions, but to provide a safety-net and strengthening rules during the crisis.

The analysis carried out in this paper shows that the crisis has generated a substantial wave of integration that seems to fit into neo-nofunctionalist predictions. Moreover, the paper has shown that a substantial political spillover has emerged in the narrow field management of fiscal rules and in a set of related policies, where the Commission has been able to profit of the crisis to strengthen its autonomy by playing upon member states divergences. In particular, while the 2011 reform of the SGP already strengthened the capacity of the Commission on delivering sanctions thanks to the introduction of the reverse qualified majority voting, the autonomy of the Commission itself was narrowed by introducing stricter fiscal targets that left little space for interpretation. The second reform occurred in 2014/2015, was grounded on the political agreement between the two major parties in the Parliament which led to the election of Juncker to the presidency of the European Commission; building the political agreement in the Parliament, the Juncker Commission was able to reshape the fiscal rules debate by introducing a flexibility clause and the EFSI. Both institutions, once considered together, constitute a substantial increase in the discretionary capacity of act of the European Commission on fiscal and economic matters; such an autonomy stems, rather than from the formal consensus of member-states, from the new role acquired for itself by the European Commission.

In the narrow field of fiscal rules, the neo-functionalist hypothesis concerning the behavior and capacities of insulated agencies of increasing their autonomy and acquiring political power seems to be corroborated, although its narrow application to the field of fiscal supervision is not sufficient to alter the general perception that crisis-led integration has been, in most part, intergovernmental in nature. Overall, the paper qualifies the claim by Fabbrini (2015) and Dawson (2015) that the New Economic Governance constitutes a mixed governance system; at this regard, the paper shows that, despite the fact that most new institutions have been built within an intergovernmental framework, a functional tension towards supranational governance is still in place and still maintains its engine in the alliance between the Parliamentary majority and the Commission, which is nowadays even strengthened by the Spitzenkandidaten process. Fiscal supervision constitutes a second instance of classical Neofunctionalist reaction to the crisis, along with the European Central Bank's wider interpretation of its mandate occurred since 2012.

However, the paper also shows that the current degree of political accountability of the Commission in front of the Parliament is likely insufficient to properly legitimize its increased autonomy in fiscal and

economic governance, due to the lack of parliamentary competence in the field. Nor this is expected to change soon: in the transition from the 2012 Four President Report and the 2015 Five Presidents Report the headline “political union and democratic legitimacy” has been shrunk, de facto, to a formal presentation of the Annual Growth Survey in front of the European Parliament and to the introduction of a common representation in international economic institutions by 2025. Moreover, the Greek crisis of July 2015 has shown how dangerous may be to maintain national competence (and hereby veto powers) on a joint economic policy which happens to be, by necessity, interconnected across the Euro Area. While “interparliamentarism”, hinted in the Lisbon Treaty (art. 8 TEU), institutionalized in the TSCG (at. 13) and advocated by scholars such as Nicolaidis (2013) and Heffler and Wessels (2013) may be considered, at a first glance, as a channel to provide “democracy”, it is in fact no closer to democracy than classical intergovernmentalism.

Both interparliamentarism (as it is enacted in today’s setting) and intergovernmentalism require unanimous decision making on fiscal and economic policy, which is a violation of the fundamental principle of democratic decision making: majority voting. Against this background, the politicization of the Commission and its (weakly) strengthened bond with the Parliament constitute the only instance of supranational legitimacy occurred in recent years and a significant, although not decisive, step forward a more efficient economic governance. Provided no Treaty change is expected to enter into force ahead of 2025, the strengthening of input legitimacy required by this newly politicized Commission relies on the informal bond between the Commission and the Parliament; at this regard, the practice of discussing the draft Annual Growth Survey in front of the Parliament, and eventually introducing amendments following the Parliament’s indications, hinted by the Commission Communication on the future of the European Semester (COM 600/2015) may represent the single most important element of legitimacy for the Economic Governance to be expected in the incoming years.



## Part Two: Postfunctionalism and the Eurocrisis



# Chapter Five: Postfunctionalism and the issue of democratic legitimacy in the era of Fiscal integration

## Abstract

While several countries still struggle to return to sustainable growth and Euroscepticism has shown its strength during the 2014 European Elections, Europe is slowly advancing on the path of fiscal integration. This paper reassesses how legitimacy is provided and why the advancing economic and fiscal integration constitutes a genetic change of the Union. The first section is dedicated to theories of legitimacy in the EU; the second section focuses on the financial and economic crisis, pointing out why some form of fiscal integration is still required to achieve a sustainable settlement; the third section sheds light on the interactions between democratic legitimacy and fiscal integration when the no demos thesis is taken into account.

Note: an early version of this paper has been published as a chapter in Krieger, T., Panke, D. and B. Neumaker (eds) (2015) *Europe's Crisis: the conflict-theoretical perspective*. Nomos Publishing, University of Freiburg.

An updated version has been accepted for publication on the *Journal of European Integration*.





# Postfunctionalism and the Issue of Democratic Legitimacy in the Era of Fiscal Integration

## 1. Introduction

European Integration, says the adage, advances through crises. Functional integration theory, in its evolution from early functionalism of Mitrany to Neofunctionalism (Haas, 1958) to neo-neo functionalism has maintained the assumption that each crisis would create the conditions to integrate at supranational level new functions. The justification for this integrative dynamics relies on effectiveness of institutions and economic advantages; further integration is often described as an “unintended consequence” (Haas, 1964) of previous measures, a step required to ensure the previous measure’s effectiveness in a changing environment. Functional integration, as described, rarely relies on the concept of democratic legitimacy; in fact, mass politics is pictured as excluded from determining integration (Hooghe and Marks, 2009). Schmitter (2002) and Haas (2003) state that only in final integration cycles would require integration of *polities* rather than *policies*; output legitimacy is the fundamental driver of EU legitimacy. Yet, the process of integration has somehow accelerated towards the uncharted territories of fiscal integration, mirrored by the rise of Euroscepticism in many countries. The slowing implementation of often-contested austerity measures and the renewed role of inter-governmentalism at European level have stimulated, once again, the debate over the alleged democratic deficit of the

European Union. Against this background, this paper argues that the EU, having entered a “Postfunctional” phase of integration, is now starting to deal with a different set of functions which require different sources of legitimacy, whose application is constrained by the relative importance of national identity.

## 2. Conceptualising Functional legitimacy

The question whether the European Union is suffering from a democratic deficit has increasingly gained scholarly attention since the decision of the *Bundesverfassungsgericht* (German Federal Constitutional Court, BVerfG) on the Maastricht Treaty in 1993. The BVerfG stressed that democratic legitimacy “is not to remain a formal principle of accountability” (Bundesverfassungsgericht 1993: 18). yet democratic deficit and legitimacy are different concepts: A political system may suffer from a democratic deficit but still being fully legitimised in front of its citizens, either because of its good policies and/or because legitimacy stems from a different level of representation (other than democratically-elected parliaments). Thus, a conclusive investigation on the alleged democratic deficit of the EU requires a two-steps process. First, it must be verified that the EU is precisely in need of the form of legitimacy that is *democratic* legitimacy; second, if this is the case, it must be verified whether such democratic legitimacy exists or not.

Legitimacy of the EU as a broader concept has been also object of intense debating. The idea that the EU relies on indirect legitimacy has obtained a wide (although not overwhelming) scholarly consensus, and it is loosely parented with both neo-functionalist and liberal-intergovernmentalist approaches. Although the scholarship on EU legitimacy is extremely rich and creative, indirect-legitimacy theses can be clustered around three main cornerstones: the “regulatory state” argument of Majone (1997); the classical principal-agent framework for international organisations reformulated by Moravcsik (2002); and the output-legitimacy argument made famous by Scharpf (1970; 1998).

The first cornerstone of a theory of functional legitimacy is given by Scharpf (1970; 1998; 2009), who applies Easton’s input- and output-legitimacy to the EU. The logic of Scharpf’s typology is, *prima facie*, quite simple: legitimacy (of a policy, of a government) can be provided on the “input side” or on the “output side”. Output legitimacy relies on the effectiveness of the policies (and thereby of the decision making process) in achieving welfare-improvements. By definition, therefore, it requires *horizontal symmetry*: in

order to be legitimized in front of all constituencies, the benefits of a particular policy should be perceived in all constituencies. A first implication of integration derived from output legitimacy is that, therefore, integration advances through series of “grand bargains” where the losses incurred by certain actors in given fields are offset by the gains of the same actors in different fields (Schmitter, 1969; 1970; 2002). Such a behaviour carries a further implication: backward revisions of any agreement are hard to achieve, even when the background conditions (or actor preferences) change (Scharpf, 1998). The second dimension of Scharpf’s legitimacy theory is the well-known *input legitimacy*, whereby the legitimacy of a government and of its policies is not ensured by the outcomes they achieve, but through the bonds that link the representatives to the governed; in a democracy, the electoral process above all. When it comes to the EU, Scharpf (1998; 2009) indeed suggests that the latter has been thus far legitimated only through output-legitimacy (the effectiveness of its decisions) rather than by input-legitimacy (the democratic election of its leadership).

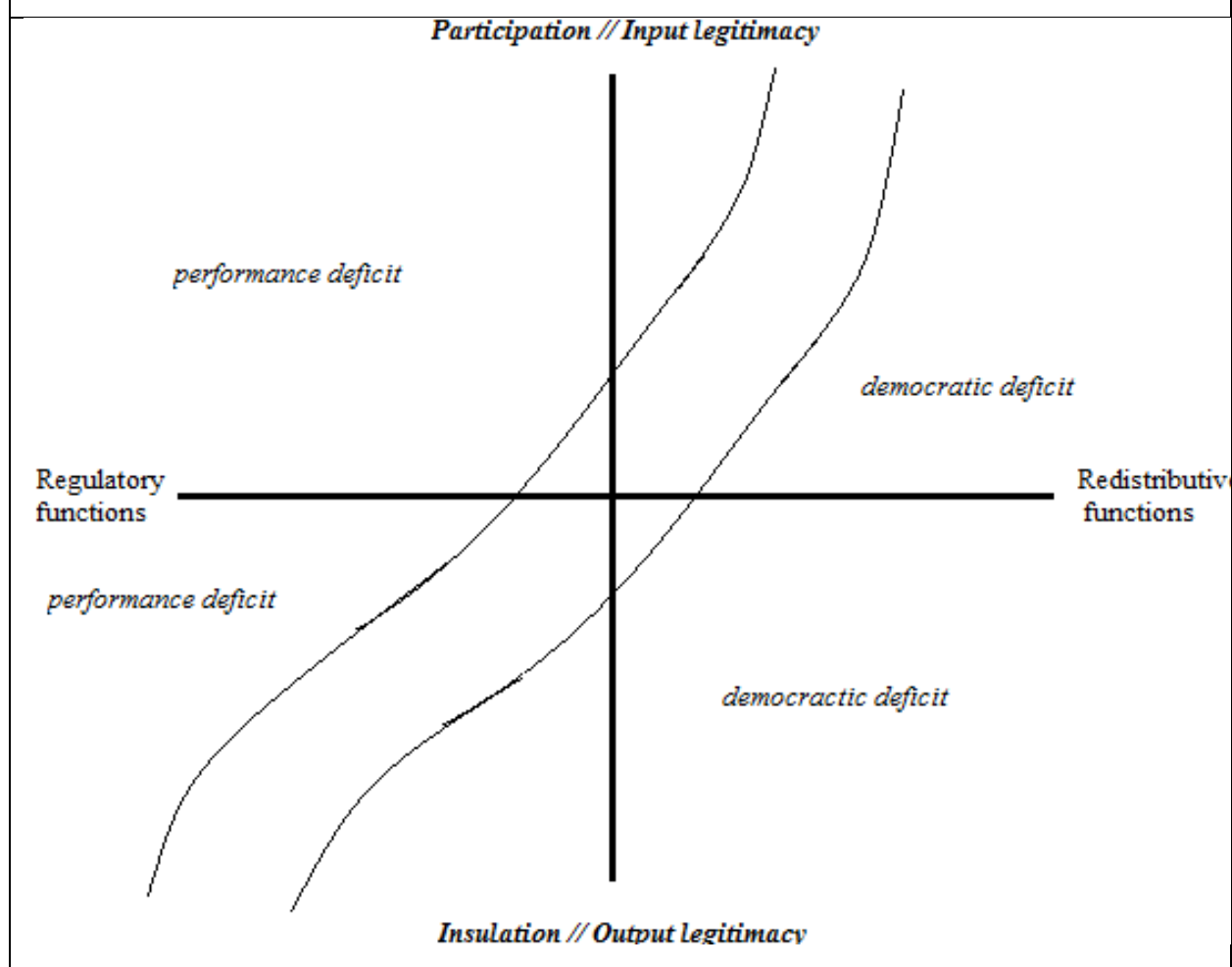
Majone (1997) further enriches Scharpf’s theorization, by arguing that democratic legitimacy is required only when the functions transferred to the supranational level entail redistributive policies among the participating countries. While this was clearly not the case before the crisis, it could have substantially changed with crisis-led integration (Majone 2014). Moreover, regulatory bodies work more efficiently when “insulated” from politics, thus strengthening output-legitimacy (Majone 1997: 4). The insulation of decision-making is thus justified, like within nation-states, by the democratic qualification of the principals, so as long as member-states preserve their democratic stance, the EU shall be considered equally democratic (Moravcsik, 2002).

These four elements, considered together, provide a solid framework for understanding indirect legitimacy. As long as the EU does not deal with redistributive policies, it does have democratically-elected principals, and it does deliver valuable outcomes for the citizens, it will be considered as a fully legitimate undertaking. Altogether, the combined arguments of Majone and Scharpf may be defined as *functional legitimacy* (figure 1): the kind of legitimacy required (input or output) depends on the redistributive or non-redistributive nature of the function under observation. It may follow that the institution under observation finds itself into *legitimacy disequilibria*: an excess of input legitimacy in policies which do not actually require it would harm legitimacy by hindering their performance (Insulation failure), while a lack of input legitimacy

in policies that require it would harm legitimacy by not adequately representing the parties, regardless of the contextual effectiveness of the decisions taken.

The legitimacy needed for a policy may be provided both on the input and the output side. Input legitimacy is more required when redistributive decisions are at stake, but may become redundant and even counter-productive –as shown by Majone’s argument- when it is not required, because it would contribute to hamper output legitimacy. There is a degree of substitution between the two components of legitimacy: particular set of policies may still be legitimated even in a situation of democratic deficit, because they produce positive effects.

Figure 1: Functional Legitimacy in theory



The stronger the democratic deficit, however, the more sensible the reactions to variations in output are expected to be. Figure 1 conceptualises this reasoning: The vertical axis represents a continuum between the two ideal-types of decision making: on one side, democratic decision making, carried out by

democratically elected bodies; on the other side, non-democratic decision making, carried out by non-elected bodies, insulated agencies, and institutions voting by unanimity. The horizontal axis represents the continuum balancing of the integrated policies; finally, the serpentine space in the centre represents the individual legitimacy threshold of each agent and of course may change over time and across regions and institutions.

It is reasonable to assume that, the more we move towards integration of redistributive policies (or essential democratic functions, as stated by the Bundesverfassungsgericht in 2009 and discussed just below), the more input legitimacy is needed. We can assume that any agent with democratic beliefs, at a certain point will think that the functions transferred to the international organization require input-legitimacy, although the preferences concerning when input legitimacy will be needed may vary. For this condition being satisfied, the level of democratic decision-making provided by the system must fall between the legitimacy threshold and the vertical axis. If it falls below, the system suffers from some degree of democratic deficit. If the system does not require input legitimacy, it must be legitimised on the output-side. However, as demonstrated by Majone and Moravcsik, protection from the influence of politicians is often a condition for effective regulatory policies: agencies often are able to deliver better results if they are insulated from constant political pressure. So, in order to have effective output legitimacy, more we move towards regulative and non-essential policies, more insulation (and less electoral decision making) is needed. Again, agents may hold different beliefs on the degree of insulation needed in a given point, but all agents believe that, at a certain point, insulation will begin to be needed in order to achieve output legitimacy. For this condition being satisfied, the level of non-electoral decision making must fall between the vertical axis and the legitimacy threshold. If it falls above, the system is experiencing a “performance deficit”: in other words, the outcomes of integration are structurally downplayed because of the excessive levels of political pressure, and output legitimacy is not achieved.

The idea that a ‘ranking’ of competences exists within democracies has also been affirmed by the jurisprudence of the Bundesverfassungsgericht. In the 2009 Lisbon Judgement, the court proposes, in fact, a list of fields of competence that *determines* the content of democracy:

“Particularly sensitive for the ability of a constitutional state to democratically shape itself

are (...) *fundamental fiscal decisions on public revenue and public expenditure*, the latter being particularly motivated, *inter alia*, by social policy considerations (...).” (Bundesverfassungsgericht 2009, para. 252, emphasis mine).

A loss of parliament’s decision making rights in these fields would not represent a marginal transfer of competences towards an institution legitimated through a classical principal-agent relation, but would instead constitute a true deprivation of substantial democracy for the concerned constituencies. As Fabbrini (2002: 24) notes, fiscal and economic policy decisions are substantially adopted today by intergovernmental decision making, while “the legitimacy of decisions taken on behalf of the EU cannot be a derivative of the legitimacy enjoyed by the governments of its member-states”. Consequently (and in absence of a body truly representative of the European people), the transfer of these competences would spoil the effectiveness of the citizens’ political rights to vote. Friedrich and Kroger (2013: 4) suggest that “(p)olitical procedures and practices are democratic if they are firmly based on political equality as the ‘foundational idea’ of democracy”. This implies that decisions shall be collectively binding and achieved by majority voting: The EU needs a shift from input to output legitimization (Habermas 2011) as witnessed by the famous *adage* “no taxation without representation”.

This is not easy undertaking. Being parliamentary control on fiscal matters essential for democracy, the Bundesverfassungsgericht notes that – when there is no parliamentary control of fiscal policy whatsoever – we are outside the democratic framework: The famous adage may then become “*no true representation* (i.e., no true democracy) *without taxation* (i.e., without control on fiscal issues)”.<sup>1</sup> If no parliament controls fiscal policy, there is no democracy. In principle, then, fiscal integration may endanger the democratic qualification of the EU: transferring fiscal powers to the EU without strengthening its democratic legitimacy would deprive the European citizens of the decision making power over an issue absolutely essential for democracy, as noted by the Bundesverfassungsgericht. Moreover, integration of redistributive policies may lead to a fundamental divergence of interests, which may drive integration towards the building up of a democratic deficit.

Naturally, many redistributive powers constitute “core state powers” which national administrations are

---

<sup>1</sup> Menéndez (2000) originally proposed the reversion of the famous principle albeit with a different meaning.

unwilling to give up; it follows that, if a pressure to integrate arises, a spill-around outcome is more likely (See Chapter 4 for reference). However, by definition, a spill-around is inter-governmental in its governance setting, lacking therefore the input legitimacy required for redistributive policies; hence the emergence of a democratic deficit and of the ensuing *negative politicization* (Schmitter, 2002; Schmitter and Lefkofridi, 2015a, 2015b). One shall note that, either way, integration of redistributive functions entails *politicization* of the integration process: either through strengthened representative institutions (“parlamentarization”) or through negative mobilization.

The classical indirect legitimacy thesis has been widely criticized. Among others, Follesdal and Hix (2006) claim that regulatory policies often entail distributive and redistributive effects not only between countries, but also within social groups. Raunio (1999) suggests that the fundamental role of governments in the EU institutions has changed the power-balance within nation-states in favour of the executive. MacNamara (2002) and Follesdal and Hix (2006) suggest that the perception of the boundaries between regulative and distributive policies may change, thus creating a democratic deficit. In particular, MacNamara – discussing the democratic oversight of the ECB – collects evidence against (1) the notion that monetary policy has no redistributive effects (MacNamara 2002: 54), and (2) the notion that central banking independence provides better outcomes in fighting inflation than democratic control over monetary policy. Finally, Agné (2007) indicates that the “chain of delegation” of the EU is both too long and not reversible, constituting a stretching and eventually a violation of the principal-agent framework and creating a deficit of democratic oversight.

The three cited arguments (redistributive effects of regulatory policies; power shifts towards executive; and ineffective delegation chain) account for the large majority of the claims that the EU suffered from a democratic deficit. Along with Majone (2014), we will argue that while these positions failed to capture the reality of European integration before 2010, the shift of sovereignty occurring since the crisis (embodied both in new institutions and new policies) has changed the nature of the Euro Area, thus producing a democratic deficit *today*. This is not due to the limits of the indirect legitimacy thesis as argued by Hix, Rauino and the other democratic-deficit scholars; rather, it is due to the accrued competences of the Union, which are redistributive in nature and require democratic legitimacy. In particular, Hix’s analysis of distributive effects in regulative policies fails to take into account the reality of EU policy-making. As



noted, among others, by Scharpf (2009), the decisions undertaken at European level should not be considered individually but rather as parts of larger packages of regulations which aim at making every participating country better off with respect to the entire regulative package. Therefore, while individual regulations may make certain countries worse off, this effect is counter-balanced by the negotiation of additional measures that are more favourable to the given country. If the whole country is better off in each round of negotiations, this implies that it disposes of resources to compensate – if it wishes so – the social groups that individually find themselves worse off. Whether it does happen or not is purely a matter of domestic preferences as represented within the national Parliament and not a defining feature of the EU construction.

Similarly, Rauinio's claim (the EU decisional procedures shift power from the parliaments to the governments) overlooks reality on the ground. In fact, countries wishing to provide a stronger level of scrutiny of executives' decisions by domestic parliaments are not prevented to do so in any way: As Rauinio himself acknowledges, certain countries have gone so far to empower national parliaments' committees to adopt binding positions for their ministries in the Council. In other words, the EU as such does not strengthen the executives *vis à vis* domestic parliaments, which can exert any control they wish; rather, executives (and not the Parliaments) are held accountable, at EU level, for their actions. In addition, national constitutional courts can intervene to protect parliamentary rights, as done by the German Bundesverfassungsgericht in 2012. It follows that, again, it is a matter of national preferences to adopt those supervisory procedures, not an institutional feature of the EU.

### **3. The impact of the crisis**

Let's now reconsider the assumption "integration advances through crises". What does it imply, in fact? Figure 1 in the previous section contributes to explain the very "engine" of European integration, its functional integration dynamics. As discussed in chapter 2 and 3, the "pace" of integration has tended to increase after periods of crisis. In a period of crisis, by definition, output legitimacy (i.e. the benefits from integration) tend to be low, precisely because there is a crisis. In other words, a crisis configures a situation of "performance deficit". If the supranational institution does not have any redistributive power, the

performance deficit can be solved through more insulated integration (left arrow in figure 2); “insulating”, i.e. providing more regulatory powers to independent supranational institutions, is precisely what the EU has done through its first 50 years of existence when facing a crisis. Therefore, if we narrow our analysis to the EU as it looked *before* the crisis, the claim that its institutions were not legitimated is weak. Not only theoretical arguments in favour of democratic deficit *before the crisis* can be, to some extent, easily dismissed; but also trust in institutions remained relatively stable until 2007, while Eurosceptic parties maintained a low profile in most countries until 2009. In sum, despite a still-lively debate, there is ground to believe that, prior to the 2009/2010 crisis, the EMU was a fully legitimated undertaking (Schmidt, 2015). However, with the outbreak of the Eurocrisis in late 2011, the output legitimacy of the European project collapsed. The first response to the European crisis, as discussed in chapter 3, was eminently “Neofunctional”: new insulated institutions and procedures were agreed, in order to address the Eurozone’s “performance deficit”.

Clearly, however, the kind of institutions and procedures needed to address the Eurocrisis were substantially different in nature from the institutions required to address previous crises. From a theoretical perspective, it has become increasingly clear, over the last few years, that the Eurozone’s institutional framework was missing the institutions, procedures and economic flexibility needed to deal with such a crisis. According to the Optimal Currency Area framework, since Kenen’s (1964) reading of Mundell (1961) a currency area is in theory enabled to prevent the emergence of crises and to correct existing crises with pure market adjustment if there is high labour and capital mobility, high prices flexibility, and reduced public debts. In the absence of these features, a currency area stuck by crisis would be endangered if appropriate institutions are not in place. De Grauwe (2007) refers, in particular, to fiscal transfers to smooth consumption adjustment and to supranational budgets to grant the effectiveness of public stabilizers even in case of national debt under stress. Direct fiscal transfers however are not the only form fiscal integration can acquire: Merler and Pisani-Ferry (2012b) show that the solution to the crisis must include either a direct fiscal union (implying both fiscal stabilizers and enforced fiscal rules), or a full-fledged banking union, or a central bank with a widened mandate. While, in principle, these are different institutions, they all imply a step towards integration of redistributive policies. Despite their functional differences, all the aforementioned options require some degree of fiscal integration; no credible solution excludes it. Fiscal

transfers between countries, by definition, require fiscal integration. A full-fledged banking union is in need of a common fiscal backstop for the joint deposit guarantee (Pisani-Ferry and Wolff, 2012); and – as shown by Sinn and Wollmershäuser (2011) and by De Grauwe and Ji (2013)<sup>2</sup> – a wider mandate for the European Central Bank (ECB) would have fiscal implications.

Alternatively, short of some degree of fiscal integration, a permanent solution to the crisis would require the overhaul of the weaker economies of the EMU through deep structural reforms aiming to re-establish the conditions that make a monetary union working without a fiscal union: price flexibility, labour mobility, low levels of public debt. However, the pursue of these goals can hardly be left to national decision-makers, who lack the incentive to promote structural reforms that can be politically costly in the short run; a system of fiscal rules (to prevent debt accumulation) and of incentives (to stimulate reforms) is needed. While establishing effective fiscal rules may address the fiscal element of the puzzle without mutualisation of resources, the provision of incentives to reform requires some degree of common funding (Economic Union). In other words, a degree of fiscal integration is likely needed even to achieve domestic solutions grounded on perfect price flexibility, structural reforms and higher mobility of factors (economic union); and indeed, the other solutions to the crisis also require the EU to move towards some degree of fiscal integration, either explicitly (fiscal union) on implicitly (banking union, ECB).

---

<sup>2</sup> With symmetrically different results concerning the direction of fiscal transfers in comparison to Sinn (2011).

Table 1 Summary of existing and proposed anti-crisis measures with fiscal implications				
<i>Function ?</i> <i>Governance ?</i>	<b>explicit redistributive consequences</b>		<b>Implicit redistributive consequences</b>	<b>Regulatory measures</b>
	<i>Temporary (loans)</i>	<i>Permanent (transfers)</i>		
Intergovernmental	<b>EFSF</b> <b>ESM</b>		<b>SRM</b>	<b>TSCG</b>
Mixed (Commission and Council/Eurogroup)	<b>EFSM</b>	Contractual Agreements ( <i>proposed</i> , Four Presidents Report, 2012; European Commission 2013) European Treasury ( <i>proposed</i> , Five Presidents' Report, 2015) <b>EFSI</b>	EDIS ( <i>proposed</i> , Five Presidents Report 2015; European Commission 2015)	<b>Reformed SGP European Semester</b>
Supranational, (insulated)		EUBS ( <i>proposed</i> , four president report, 2012; European Commission, 2014)	<b>OMT; QE</b>	
Supranational, (co-decision)				
<i>EFSI</i> : European Fund for Strategic Investments ("Juncker's Fund") <i>EUBS</i> : European Unemployment Benefit Scheme <i>EDIS</i> : European Deposit Insurance Mechanism <i>SRM</i> : Single Resolution Mechanism				

Since 2011, the EMU has shown some progress: it has created a series of bail-out mechanisms, it has introduced strengthened coordination of fiscal and economic policies through the Six Pack and the Fiscal Compact; it has introduced the first two steps of a banking union (still lacking a joint deposit guarantee); and it has changed its monetary policy to the point that an implicit guarantee on public debt is de facto in place; it has introduced an investment instrument to boost growth. Many of these measures have direct or implicit redistributive effects, either on a (theoretically) temporary basis (through loans) or permanently (through ECB's debt purchasing or through EFSI (European Fund for Strategic Investment) grants and contributions.

However, none of the instruments introduced since 2011 is tailored to provide shock-absorption or redistributive functions (albeit several instruments proposed, but not yet implemented, have this aim); nor any of the introduced instruments provides incentives for structural reforms at domestic level. Moreover, none of the instruments introduced is endowed with a supranational democratic governance (table 1): when the governance system is supranational (like in the case of the OMT and of the EFSI) the decisions are taken by Commission or ECB officials without Parliamentary consent; in other instances, either the system

is purely intergovernmental, or the Commission and the Council share the decisional burden, but without involvement of the European Parliament.

It is reasonable to assume that the Eurozone design is not yet in equilibrium and will be modified again in the future, but the same shortcomings seem to apply to the measures formally proposed thus far to strengthen EMU's fiscal integration. As indicated by the Five Presidents Report (2015) and by several national proposals (including the Bundesbank-Banque De France proposal for a Eurozone Financial Minister, 2016). In fact, the policy debate is beginning to align with theoretical prescriptions concerning the need of EU-wide stabilization instruments (for instance, a European Unemployment Insurance- Claeys, Darvas and Wolff, 2014; Beblavy, Marconi and Maselli, 2015). Perhaps, rather than a question of "if", is a question of "when" a limited degree of explicit fiscal integration will be introduced in the EMU design, either as a tool for stabilization, or as incentives to reform.<sup>3</sup>

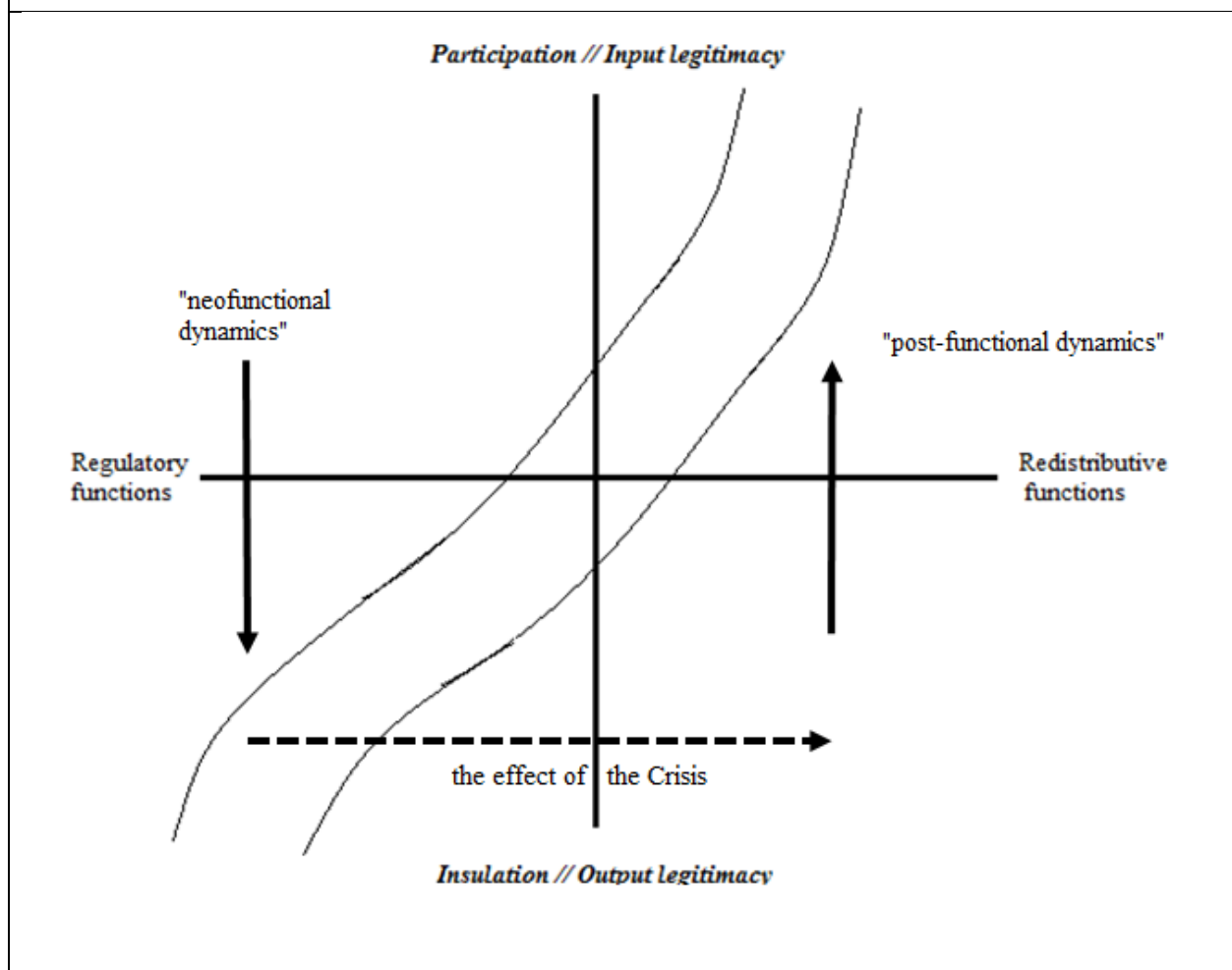
Fiscal integration touches the very core of democratic systems, whose Europeanisation – either in the form of a strengthened cooperation or with a full transfer of competences – does not simply represent a marginal incremental change in the EU competences. Rather, it constitutes a paradigm shift in the nature of the EU and in the way the EU itself shall be legitimised; nevertheless, the instruments formally proposed by EU bodies, so far, lack democratic legitimacy (table 1). Figure 2 reconstructs the "paradigmatic shift" into the functional integration diagram introduced in the previous section: the effect of the crisis "moves" the Eurozone from the bottom-left corner, with rather insulated institutions legitimated on the output-side through their performance in fulfilling regulative functions, to the bottom-right corner; the (slow) introduction of redistributive measures also introduces a previously absent "democratic deficit".

The slow but continuous process of fiscal integration generates controversial effects. On the one hand, it is not sufficiently strong to re-establish European-wide output legitimacy (albeit in a non-democratic framework). On the other hand, the first elements of the new economic governance aimed to constrain domestic behaviour and increase the power of insulated institutions in fiscal matters, generating a democratic deficit.

---

<sup>3</sup> Implicitly, fiscal integration is already in place through the ECB balance sheet and the upcoming Single Resolution Fund.

Figure 2: functional legitimacy in the Eurocrisis



In other words, Current EU anti-crisis measures, while having limited European-wide redistributive effects (no output legitimacy at EU level), greatly reduce the space of action on economic policy of national lawmakers, constraining their capacity of enacting redistributive policies at domestic level (Scharpf 2012:22). By doing so without successfully addressing the crisis, the EU has both reduced its output legitimacy (Schmidt 2015) and hindered the input legitimacy of national governments (Scharpf 2012:18), contributing to the rise of Eurosceptic parties in several countries (See Chapter 7, or Nicoli 2016).<sup>4</sup>In other words, the crisis has created a “twin legitimacy deficit” of European integration, failing to integrate sufficient redistributive policies to achieve output legitimacy, but sufficient progress towards insulated

<sup>4</sup> While, as suggested by Scharpf (2012, 2014) the EU output legitimacy has evolved unevenly depending on the different outcomes of European economic policies, it must be noted that support for Eurosceptic parties is generally on the rise also in countries which have been less hit by the crisis such as the Netherlands or Austria.

decision making on fiscal policy to fail to reach input legitimacy. While “performance deficit” drove the Neofunctional stage of integration towards the construction of insulated institutions, democratic deficit is likely to be the driving force of the Postfunctional phase of integration.

I therefore argue that the Euro Area is now in a “grey zone”: having introduced some limited forms of fiscal integration, it is not anymore a simple currency area, and therefore output legitimacy is (in theory) increasingly not sufficient; moreover, given that the progress in fiscal integration has been partial, its effectiveness in addressing the structural problems of the EMU on a permanent basis is limited, further undermining (in practice) output legitimacy. In other words, the EMU is stuck: given that it has begun to progress towards fiscal integration, the EMU democratic qualifications would greatly benefit by some more input legitimacy, but it could keep relying on output legitimacy, given that fiscal integration has been partial; however, precisely because integration has been partial, output legitimacy is vanishing both domestically and at European level. To re-establish output legitimacy integration should go forward towards the completion of fiscal integration, but if this were to happen, then, output legitimacy would not be sufficient if the EMU is to remain a democracy (at least according to the Bundesverfassungsgericht’s understanding of democracy). However, while output legitimacy on fiscal issues would violate the democratic condition of political equality, the introduction of input legitimacy can hardly be handled without raising problematic issues. At the same time, as noted by the Bundesverfassungsgericht in 2009, the simple transfer of fiscal power to the European Parliament would not preserve the political equality criterion, as the European Parliament is elected based on geographical constituencies with a regressive proportionality principle, and there is no second federal chamber where the equality of states is represented (Bundesverfassungsgericht, 2009, para. 274 and following).

#### **4. The *no demos thesis* and its implications**

More importantly, the transfers of economic and fiscal powers to a supranational assembly<sup>5</sup> would be insufficient if we maintain that identity is a precondition for democracy when democracy has redistributive

---

<sup>5</sup> This holds even when respecting the criteria laid down by the Bundesverfassungsgericht, for example, by creating a federal parliament where people are represented both as citizens of a state and as individuals.

implications. The relationship between redistribution and collective identity has noble fathers in political philosophy: It can be perceived already in David Hume's theory of morality as described in the *Treatise*, which assumes that one's feelings intensity for another human being increases as one's proximity to the individual strengthens (Cohon 2010, para. 7), thus justifying stronger redistributive policies within nations than between. Ferdinand Tönnies' *Gemeinschaft* concept also reflects the idea of societies built upon shared community beliefs rather than upon rational contractualism. In the second half of the twentieth century, the debate over the societal boundaries of democracy and redistribution has revamped on both sides of the Atlantic. In North-America, the renewed discussion addressed the issue of the origins and limits of redistributive justice, being marked by contributions like Rawls' *A Theory of Justice* (1971), MacIntyre's *After Virtue* (1981) and Walzer's *Spheres of Justice* (1983).

In Europe, the debate – ignited by the Controversial Maastricht decision of the Bundesverfassungsgericht in 1993 – focused on the limits of a democratic transformation of the European Union alongside the emergence of a collective European Identity. In this context, the so-called *no demos thesis* was developed, among others, by Bryde (1994), Kielmansegg (1994; 1996), and, to a lesser extent, by Grimm (1995), Weiler (1996; 2000) and Zürn (2000). As Zürn writes, the foundation of the no demos thesis is that “majoritarian decision-making is hardly achievable beyond the national level since it requires some form of collective identity that includes trust and solidarity” (Zürn 2000: 195). Some proponents of the thesis, like Bryde (1994), ground the *demos* into ethnical, linguistic and cultural features, which create links of solidarity among the demos members, thus justifying redistribution through majority voting. Outside the demos, these boundaries disappear, making the deployment of a working democracy impossible. Naturally, the no demos thesis is controversial: for instance, Habermas has long argued that citizenship can be anchored in *constitutional patriotism*, rather than in communitarian identity.<sup>6</sup>

Weiler's<sup>7</sup> depiction of the no-demos thesis is likely the most articulated: “democracy does not exist in a vacuum (...) if there is no demos, there can be no operating democracy” (1996: 523). The nature and the ultimate goal of the European constitutional construct (its *telos*) is indeed not to proceed towards the

---

<sup>6</sup> At the European scale, the contrasted communitarian identities are the national ones. At national level, naturally, the communitarian identities at stake are the regional or pre-national ones.

<sup>7</sup> Weiler's position on the argument has evolved over time from an initial sceptical position (1995) into a moderate agreement (1996) and finally towards his “constitutional tolerance” approach (2001).



creation of a single European demos, but rather to preserve peacefully the distinct demoi.<sup>8</sup> Consequently, a true majority-voting democracy at EU level is not possible, and the departure from the unanimity vote procedures occurred with the Single European Act coincides with the beginning of the crisis of the European construction: “no matter how close the union, it is to remain a union among distinct peoples” (Weiler, 2000: 14).

The no-*demos* argument, as reconstructed by Weiler, is composed of a positive statement (“Europeans are not a *demos*”) and a normative claim (“Europeans shall not become a *demos*”). While the normative claim is controversial, many citizens (including committed Europeans) and political leaders would likely agree with the positive claim. For instance, the Bundesverfassungsgericht (2009, para. 279) writes: “The democratic fundamental rule of the equality of opportunities of success (“one man, one vote”) only applies within a people, not in a supranational body of representation, which remains a representation of the peoples linked to each other by the Treaties.”

In a way, the 2009 ruling on the Lisbon Treaty constituted an extraordinary compendium of the defining principles of classical democracy, providing a (legally binding) interpretation of the relations between the fundamental political competences of sovereignty, parliaments, *demos*, and representativeness. The Bundesverfassungsgericht appears to share the positive part of the no demos thesis concerning democracy, including the basic arguments for which democracy (majority-voting) is possible only within one demos. Although the Court does not rule out the emergence of a European demos, especially through institutional reforms, it recognises that such a demos is still yet to emerge; and thus only inter-governmental politics are possible provided the existing institutional balance. However, the Bundesverfassungsgericht reverses the classical argument of the no demos proponents: it is democracy, defined by political equality and its essential functions (like fiscal and economic policy) that defines the demos. Where individuals enjoy political equality and their decisional power concerns essential democratic functions, then we have democracy and thus the demos is established.

---

<sup>8</sup> “Europe is not yet a Demos in the organic national-cultural sense and should never become one” (Weiler 1996: 528).

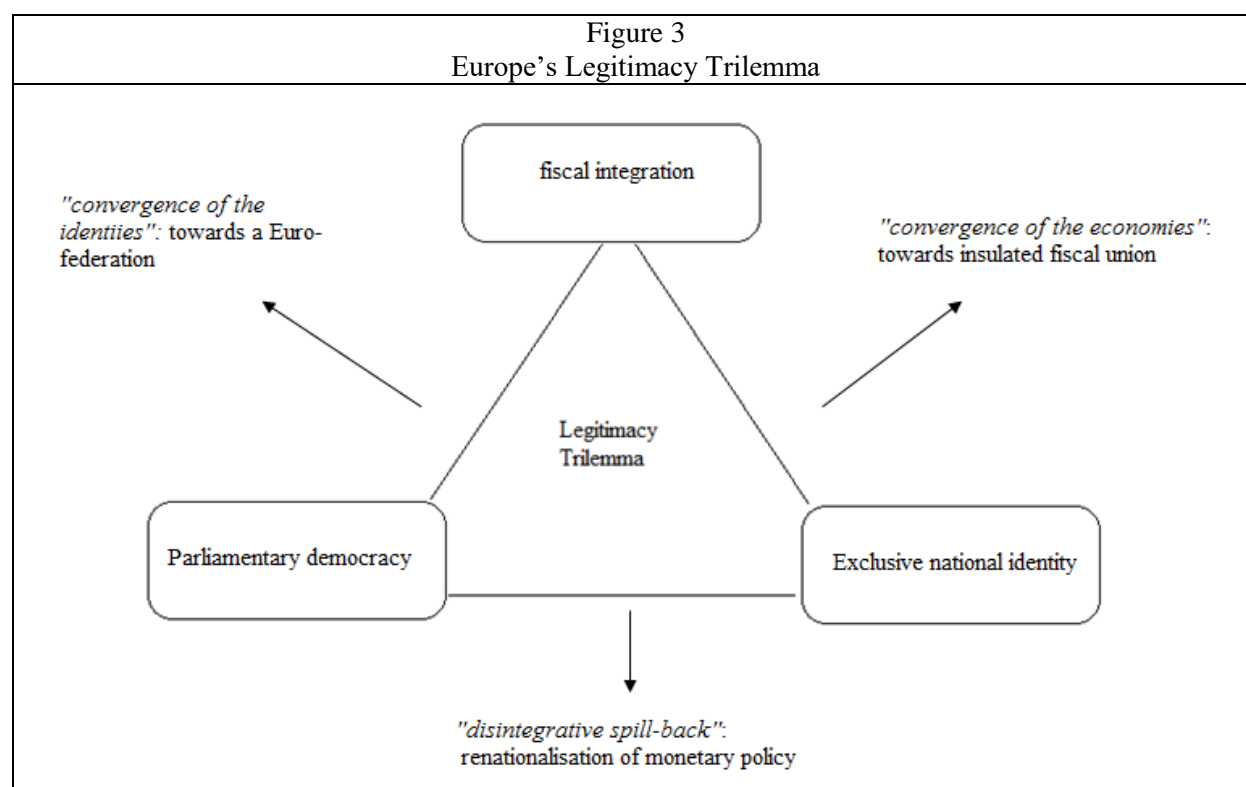
## 5. A legitimacy trilemma

In light of the no demos thesis, the lack of shared European identity generates a major issue: either we decide to proceed in securing the EMU with fiscal integration giving up any claim of democratic control over it, thus creating a purely inter-governmental (output-legitimized) fiscal union; or we decide to maintain democracy at the national level, avoiding fiscal integration, and therefore receding from monetary integration. In other words, the EU is facing a true *governance trilemma*, which may be resumed by Figure 3 (briefly introduced, already, in Chapter 2). We can preserve democratic decision-making, the monetary union, and exclusive national identity, but only two of these features at a time. Pursuing all three features simultaneously would prevent any resolution to the crisis. In fact, democratic decision making and fiscal integration are consistent, but this would require the creation of a European Parliament that is enabled to deal with fiscal and economic policy. This would be in contrast with an exclusive national identity, which assumes that fiscal policy cannot be the object of democratic decision making outside the demos because of its redistributive implications. Similarly, we could maintain an exclusive national identity and proceed towards fiscal integration at the condition that any decision on fiscal and economic policy that is undertaken in the newly established fiscal union is taken by consensus of governments, thus removing democratic decision making from controlling these policies. Finally, we could maintain an exclusive national identity and a majority-voting control over fiscal and economic policies, only if these are not integrated at the EU level. The next sections will discuss each of the alternatives in more detail.

The paper previously showed that the EU was not in need of direct democratic legitimacy *before the crisis*, so the question whether the EU suffered a democratic deficit was, at the time, redundant. However, we also showed that the post-crisis integration, concerning fiscal and economic policies, could not be insulated any longer. Today, the range of policies undertaken at EU level does need democratic legitimacy. If the EU is not able to provide it, it would suffer a democratic deficit. However, if confronted with the no demos understanding of democracy, we end-up being trapped in a trilemma with no apparent way out.

The implications for the European Union and its quest of legitimacy differ under each of the different options. From this point onwards, we enter a rather uncharted territory. While figure 1 may look familiar, it differs in some fundamental elements from the global economy trilemma proposed by Dani Rodrik (2007;

2011) and operationalised by Crum (2013) for the Euro Area.



The legitimacy trilemma proposed here, albeit dealing with a comparable set of problems, differs in three fundamental aspects from Rodrik/Crum approach.<sup>9</sup>

First, the domain of effectiveness of the legitimacy trilemma is extremely restricted when compared with Rodrik/Crum's own approaches. In section A it was demonstrated that not any level of "globalization" threatens democracy, but only sufficiently advanced degrees of integration that put redistribution at stake.<sup>10</sup>

While this may sound trivial at a first glance, it is worth noticing that in Rodrik's setting, functional integration is never compatible with democracy; the European project seems to be in conflict with

<sup>9</sup> Rodrik's (2007) trilemma features globalization, democracy, and the nation state; Crum (2013) operationalization features the Euro, democracy, and national determination.

<sup>10</sup> This may change across time and societies. As noted by Moravcsik (2002: 614), although monetary policy might have redistributive implications, it was possible to create the ECB because the redistributive function of monetary policy was widely rejected at the time of its creation.

democracy since its inception, as Rodrik's conceptualization excludes a theory of output legitimacy and relies exclusively on parliament's control to define democracy. This paper instead argues instead that (i-along with the Bundesverfassungsgericht) only integration of fundamental democratic functions defines democracy; and (ii-along with Schmitter, 1970; 2002), that only the final phase of integration, putting redistributive policies at stake, requires a leap forward from *integration of policies* to *integration of polities* (Haas, 2003).

Second, the concept of nation state as a *vertex* of Rodrik's trilemma is fully misplaced. A fully sovereign Nation State constitutes already a political system in "functional equilibrium" (Schmitter, 2002) where all key competences of sovereignty are maintained at the same governance level (Genschel and Jachtenfuchs, 2016). In a Nation State with full fiscal and monetary sovereignty, very strong sense of identity, and working democratic institutions, there is no trilemma. However, if a nation-state were to lack common identity, then the trilemma would arise even *within* a nation-state, regardless of the degree of external globalization. Similarly, if Europe had these three elements together, there would be no trilemma, regardless of whether it acquires the status of a "State" or not.

In other words, a nation-state (a democratic state with all core state competences and a coherent national identity) rather than a vertex of the trilemma (like in Rodrik, 2007), constitutes *a solution* of the trilemma. Classical Nation States, being the milieu of redistributive politics in a geographical area occupied by a single "people" constitute one the trilemma's possible solutions; in classical Nation-States the trilemma is solved by creating a single demos kept together by a strong bond of identity, hence nullifying the *no demos thesis*. In Rodrik's setting Nation States constitute a vertex of the trilemma, but at this point of the analysis it should be clear that relinquishing national sovereignty without addressing the identity issue does not solve the trilemma at all; it rather generates new problems, as witnessed by secessionist pushes in existing nation-states with sizeable minorities (i.e. lacking a common identity). A proper vertex for the trilemma, instead, requires "exclusive national identity"; solving the trilemma for integration and democracy requires the creation of a degree a shared identity, overcoming the exclusiveness on the national bond.

Following the original Rodrik's setting, a European Federation would constitute a solution to the same trilemma on a larger geographical area, regardless of the existence of some identity bond between its

participants; it is simply a matter of allocation of functions to the right level of governance, as if functional integration could shift seamlessly from non-redistributive to redistributive functions. In the setting here proposed, a European Federation, if not grounded into a “self-understanding” of a European people, would result in increased detachment, Euroscepticism and resentment against the European integration process, as suggested by Haas (1964) and Etzioni (2001) and not differently from what already happens in several existing nation states struggling with regional independence movements.

Finally, a third reason to believe that the legitimacy trilemma here proposed is better suited to model the Euro Area problems than the Rodrik/Crum setting, is that the setting proposed here is grounded on well-established theoretical work. Fiscal integration (of some kind) as a solution for un-optimal currency areas has been discussed since Mundell (1960, 1961), Kenen (1969) and several European Commission reports (Werner, 1971; McDougall, 1977; Padoa-Schioppa, 1987; Delors, 1988) and constitutes one of the cornerstones of today’s debate on European economics; the idea of democratic legitimacy and redistribution is widely discussed since Majone (1997) and adopted by the Bundesverfassungsgericht in 2009; the same Bundesverfassungsgericht contributed, since 1993, to the lively debate on the *demos* thesis.

For these reasons, even if Rodrik’s work may provide some insights concerning the long-term outcomes of the trilemma’s pairs, it is insufficient to provide a correct understanding of the crisis of the European Union. A discussion of the trilemma’s solutions follows in the next sections.

## **6. national identity and democratic principle: a “disintegrative spill-back”?**

The first option for resolving the trilemma implies the choice of democracy and exclusive national identity, therefore rejecting fiscal and monetary integration. Is the dissolution of the Eurozone a viable option? As discussed below, theory and historical experience seem to suggest that the dissolution of monetary unions would not move the institutional-economic system into a stable equilibrium. Further institutional adjustment would be needed, endangering the European Union and the Single Market.

What are the implications of a Euro-breakup? Besides the short term effects of a similar decision (which according to several studies – UBS [Deo et al. 2011] and Bertelsmann Stiftung [Belke 2012] – might acquire a global magnitude several times higher than the collapse of Lehman Brothers), removing the Euro would

endanger the long term stability of the EU as a whole, possibly unleashing a dis-integrative dynamics of the EU. The EMU, in fact, was introduced for specific functional reasons, as discussed in Chapter 2. While there was a sincere political willingness to push forward European integration, there was also a clear macroeconomic concern behind EMU inception: achieving a sustainable monetary stability in Europe to prevent the collapse of the Single Market. Both attempts to create a quasi-fixed exchange rate system after Bretton Woods (the “Monetary Snake” and the European Monetary System) had collapsed; a common currency was (and is) required if fixed exchange rates (needed to prevent exploitation of the common market rules) and capital mobility (at the heart of the single market agenda in 1985-1992) are to be kept together. In other words, the Euro is the only possible solution to Mundell’s (1961) famous “Impossibility Trilemma” in favour of free movement of capital and fixed exchange rates (thus repelling independent monetary policy). The collapse of the EMU would raise the same question again, namely how to create monetary stability in Europe, without a viable solution. With divergent monetary policies, a fixed exchange rate system is not tenable; therefore, further disintegration may ensue, endangering the Single Market for goods and capitals. Without trade barriers, in fact, countries with higher inflation preferences may be tempted to depreciate their currencies in order to boost short-term price competitiveness, adopting a beggar-thy-neighbour policy; as a consequence, the preference in favour of trade openness in the other countries may collapse, endangering the Single Market. From this perspective, it is straightforward to understand the pressure that the European single market for goods would suffer in case of a dismantling of the Eurozone: a disintegrative decision on the third trilemma (legitimacy) would prevent a forward-looking solution on the second trilemma (monetary) thus generating pressure on the first (trade).<sup>11</sup>

## **7. Monetary union and national identity: “convergence of the economies”**

The second choice with respect to the legitimacy trilemma concerns monetary union and exclusive national identity, leading to an inter-governmental type of fiscal integration (or executive-federal in the words of Habermas). Clearly, it would produce a shift from input (democratic) legitimisation to an output legitimisation of fiscal policies. Indirect legitimacy for insulated institutions worked as long as the EU could be qualified as a regulatory, non-redistributive polity, but adding the redistributive functions would

---

<sup>11</sup> Chapter 2 provides a detailed reconstruction of the process of economic integration as a series of sequential trilemmas.

constitute a fundamental change of the Union and, if pursued without democracy-enhancing reforms, would constitute a net loss of democratic stance (Majone 2014). Nevertheless, such arrangement may work in practice. In this setting, the formal equality of states, including their veto powers on fiscal matters, shall be preserved in respect of exclusive national identity. However, the credibility of commitments is still essential: Credibility must cover not only the willingness of peripheral countries to adopt reforms, but also the willingness of core countries to pay. If each fiscal transfer were to need 28 majorities in 28 national parliaments, the whole system would end-up being completely non-credible in face of financial markets and of the voters. Moreover, the whole ‘grand-bargaining’ still needs to be protected by electoral politics. Fiscal and economic integration (with legal responsibilities for both net recipient and net contributor countries) is thus again insulated and protected by unilateral changes through constitutionalisation in a fiscal treaty with redistributive features. Indeed, the “insulation logic” observed by Majone constitutes not only a requirement to achieve effectiveness avoiding decisional traps, but also a strategy to ensure compliance (Wolf 1999: 341). The goal is precisely the *de-democratization* of a given competence. The respect of national sovereignty turns a purely fictional stratagem into an insulation setting. Clearly, the respect of the no demos thesis is apparent: In order to grant to each national demos equal and non-majoritarian rights on fiscal and economic policies, these policies must be excluded from the fields of action of democratic policy-making and being constitutionalised. Such an arrangement, albeit eventually effective, would face two major problems on the legitimacy side. First, constitutionalisation of fiscal policy strengthens Vivien Schmidt’s (2006) paradox: the EU adds a new “policy without politics”, and MS lose their core policy for politics to deliberate on.

Second, precisely because the new-born fiscal policy is insulated, it would be legitimated on the output side. However, the benefits (output) should be positive across the different constituencies in order for the agreement to remain legitimated. In other words, output legitimacy requires *horizontal* effectiveness of the implemented policies. This requirement generates two problems: how to deal with (1) variations of constituencies’ interests and preferences after the constitutional agreement, and (2) time inconsistency issues?

In an intergovernmental setting, we can assume that, if an insulated policy was agreed upon in the first place, the ex-ante expectation is that it would produce positive results in all the parties agreeing upon it

(either directly or as a part of a “grand bargain”). However, if that policy ends up producing welfare losses in a given constituency, output legitimacy is not achieved- as suggested by Scharpf (2012, 2014) the lack of horizontal effectiveness during the Eurocrisis hindered the output legitimacy of the EMU. Therefore, insulation is not an agreement about the rules of the game, but about the winners of the game, which in theory should be *all the involved constituencies* for true horizontal output legitimacy to be achieved. Of course, no constituency would (in theory) agree with a ‘quasi-constitutional’ agreement that is structurally against its interests. During the negotiations, the delegates would use their veto powers to block any agreement that does not respect (overall) their own preferences, so the loss of democracy experienced by the constituency that is bound by the agreement is matched with material gains, thus providing output legitimacy. For a single fiscal or economic decision to be output-legitimised, therefore, a relevant level of ex ante economic convergence is required, not only because it would be unlikely that the insulated institution would be endowed with powers of taking a decision structurally against the interests of a constituency, but also because if this were to happen, that decision would still not be output-legitimized in the losing constituency. Now, provided that fiscal and economic integration are a requirement for further convergence in the EMU, we also face a problem of time inconsistency: can we legitimise economic and fiscal integration with a source of legitimacy (output legitimacy) requiring, to be effective, horizontal effectiveness, and therefore ex-ante convergence, which in turn requires ex-ex-ante fiscal and economic integration?

Temporal expectations play here an essential role. Agents may support losses in actual democratic stance only if concrete advantages show up timely. The higher the loss, the faster results shall be delivered.<sup>12</sup> Naturally, the ‘timely’ definition may vary across regions and individuals: Some may accord high values to short terms gains, while others may prefer long-term advantages. However, as explained above, these arrangements are credible only if we focus on the long term, that is, if their content does not depend on the national political cycle.<sup>13</sup> It follows that, in order achieve an appreciable degree of output legitimacy in the

---

<sup>12</sup> Empirical studies on the European Identity and the legitimacy of the institutions demonstrate that there is an extremely sensitive component in the individual attitude towards EU institutions in relation to short-term achievements (see Bruter 2003: 116).

<sup>13</sup> In practice, as long as multiple constituencies exist, and as long as these constituencies hold different interests, it may be difficult to find an agreement that satisfies the long-term commitments condition and the short-term effectiveness condition for any constituency.



long run, an insulated fiscal and economic Union would have to deploy substantial instruments to foster convergence in the short term, thus enhancing long-term horizontal effectiveness (and thus widespread legitimacy) of a common insulated fiscal policy.

#### **8. Monetary union and parliamentary democracy: “convergence of identities”**

There is a third possible outcome of the trilemma, a *federal* integration pattern combining supranational democracy and monetary union. Several concerns can be raised, however, despite the clear political appeal of such an option. These concerns rely on a simple observation: creating a shared European identity is a complex task. There is little doubt concerning the fact that Europeans are not (yet) a ‘people’; integrating further may strengthen the hand of hard-line Eurosceptic parties, and –not differently from many democratic fiscal federations like the UK, Spain and Belgium— the EU would suffer widespread secessionist pressure. Even functionalists with rather federal feelings, as Haas (1964) and Schmitter (2002), consider a quick federalisation of the EU unlikely to happen without traumas. The former, in his analysis of international integration patterns, considers that federal integration would succeed only after the instauration of a “liberal nationalism”. In other words, after a conflicting phase between original national identities, the supranational authorities may succeed to build up a true federation overcoming the nationalist oppositions with the creation of a strong and shared body of beliefs and values. In addition, Schmitter considers that governments would resist with some forms of “power protectionism” boosting national identities.

Identities, however, are not fixed in the hyperuranium: they can evolve over time and they are constructed through a dialogical process; an appropriate configuration of the political arena may provide the space for a shared identity to emerge endogenously. If the power of an elected assembly (such as the European Parliament) over fiscal issues is increased, then political parties will increase their efforts to take control of the assembly, investing more in collecting votes, mobilizing consensus and building up organizational structures. Because of the organizational efforts and the search for consensus, two effects are likely to arise: (1) increased political polarization, and (2) increased participation rates in the elections. At this regard, Hix, Noury and Roland (2007) recognise that a relevant increase of the parliaments’ powers to shape the

outcomes of the political process can indeed increase their legitimacy. Furthermore, a strengthening of the Spitzenkandidaten process, and a stronger link between the results of the European Elections and the economic policy enacted at EU level, may contribute to the process: the introduction of a true parliamentary control over fiscal and economic policy at EU level would create the incentive for the construction of collective preferences. For instance, amending existing provisions on the Economic Dialogue within the SGP legislation, and endowing the European Parliament to take an active role in the drafting of the Annual Growth Survey, not only would not require treaty amendment (only secondary legislation change) but also would contribute to set up the institutional conditions for the emergence of an endogenous dynamics of identity-building through the political process.

Moreover, two indirect endogenous dynamic may emerge. First, economic preferences are an important part of our collective identities: an appropriate European-wide fiscal and economic policy may foster economic convergence, thus generating a re-alignment of economic preferences and creating the foundation of a shared identity. Second, those who enjoy the benefits of integration may also start to feel more European; along with classical Neofunctionalism (Haas, 1958) as integration produces benefits, identities and allegiances to Europe are built. Following this path, even if an early decision on “non-democratic” fiscal and economic integration is made, the ensuing convergence of the economies may entail convergence of (part of) our identities as well, making easier to introduce democratic provisions later in the process.

## **9.      *Conclusions: convergence of the identities or of the economies?***

The European integration process has now reached a third stage, a “transforming cycle” in Schmitter (2002) words. As Genschel and Jachtenfuchs (2016) suggest, the dynamics is now heading towards the remaining core state powers left at national level, fiscal and economic policy making in particular. The paper has shown that while talking of a democratic deficit before the crisis may have been redundant according to both theoretical reasoning and empirical evidence, the wave of crisis-led integration that occurred since 2010 is changing the picture. The EU is not simply facing the need for further democratization: Instead, we show that the Union is trapped in a policy and legitimacy deadlock from which there are no easy ways out. Fiscal integration, coupled with enhanced supervision of domestic fiscal and economic policies, is, probably unavoidable if monetary union is to be maintained. However, fiscal integration will substantially transform

the Eurozone into a redistributive polity. Depending on the institutional setting, the ensuing conflict could either be qualified as a national struggle or as a societal struggle. Similarly, inaction will equally fuel social conflict, as indicated by the rising populism in many EU member states.

The analysis suggests that the EU is caught in a ‘functional trap’: none of the possible choices is costless. Dismantling the Monetary Union not only could push the continent towards a new financial disaster, but also release disintegrative dynamics which ultimately would end only with the collapse of the Single Market for goods and capital. Proceeding with output-legitimated fiscal integration (thus avoiding federalism and the political costs it entails) would require a substantial convergence of the economies, so that horizontal effectiveness is achieved. However, such a solution may have huge costs in terms of democratic legitimacy, may fuel national conflict and may constitute a solution not lasting sufficiently long to achieve true economic convergence.; the risk that short- and medium-term losers of such process would rebel before accessing long-term gains is high. Finally, a federal integration pattern would need convergence of the different identities to achieve effective input legitimacy. Constructing a fiscal federation without a degree of shared identity is risky as it will require a democratically legitimised sharing of resources among communities that do not have a truly unified public sphere, identity, or sense of common belonging. Experience shows that this is hard to achieve without political conflict and potential break-ups even within long-standing established communities.

At this regard, a key question still unanswered concerns the resting point of both further integration and disintegration solutions on the trilemma. Once unleashed, a dis-integration dynamics may be hard to stop, due to the incremental nature of European functional integration. However, it equally uncertain whether an adequate protection of democratic legitimacy is possible if further integration is achieved without a strengthening of a common European identity. Yet fiscal integration is on the way; and it is unclear for how long “fiscal policies by stealth”, mediated through the ECB balance-sheet, can be maintained. At this regard, the Bundesverfassungsgericht pointed out, in its decision of June 21<sup>st</sup>, 2016, that the legality of the OMT is subject to conditionality and must be reversible once the crisis is finished. Moreover, Mr. Draghi himself pointed out in several occasions that the ECB action is temporary and that governments have to take the lead in fiscal integration. With 2025 in sight, policy makers should be aware of the risks entailed with each of the possible choices over the trilemma. Finding a source for a shared European identity seems

a central priority and a condition for further integration. Alternatively, the EU risks facing the emergence of a dysfunctional system hostage of minority blockages in national parliaments and characterised by recurrent instability on the financial markets. Ultimately, such sub-optimal solutions may not be sustainable and may end up provoking the collapse of the EMU.



## Chapter Six: Powers, Governance, Eurobonds. Did the crisis affect preferences for integration?

### Abstract

The Eurocrisis has generated a wave of new institutions and policies. Yet, the agenda for the reform of the Monetary Union has no lack of measures waiting for member states approval. During the crisis, however, a substantial cooling of the public opinion in favour of more integration has been observed. Against this background, the paper seeks to clarify if and to what extent the Eurocrisis has affected preferences for further fiscal integration through a country-level panel dataset built on 10 waves of Eurobarometer data, and 3 different measures of fiscal integration.



# **Powers, Governance, Eurobonds: did the crisis affect preferences for fiscal integration?**

## **1. Introduction**

Since the outbreak of the Eurocrisis, in 2010, the European Union and the EMU in particular have witnessed no lack of integration. The Euro Area has introduced nothing less than: three new Treaties (Treaty on Stability, Coordination and Governance-TSCG; the European Stability Mechanism treaty; the Intergovernmental Agreement on the Resolution Fund); one treaty amendment aimed at weakening the no-bail-out rule; two new procedures (European Semester, Excessive Imbalances Procedure); the first two pillars of a Banking Union; a change in mandate of the ECB. In spite of all new institutions introduced, the Brussels' appetite for further integration has not substantially decreased, as witnessed by the 2012 Four Presidents' Report and the 2015 Five Presidents Report. A key question, however, remains largely unanswered: to what extent the preferences of citizens and governments have evolved, during the Eurocrisis, to back further integration? A few studies have attempted to provide an answer, lacking, however, either a sufficiently comprehensive breath to fully catch the multi-dimensional nature of the phenomenon, or a sufficiently extended time dimension. Against this background, this paper analyses the impact of the Eurocrisis on preferences with a quantitative approach. Panel level econometrics is used to,



study the impact of the Eurocrisis on citizens' preferences for further integration on three dimensions: first more general preferences for integration to solve the crisis; second, specific preferences for further strengthening of the EMU economic governance; third, preferences for Eurobonds, a specific form of fiscal integration for which data have been coherently collected over time. In all three cases, data are obtained from pooling together 12 Eurobarometer data series, from 2011 to 2015. The paper is organised as follows: section 2 lays down the theoretical framework and the leading hypotheses of the study; section 3 discusses data and methodological issues; section 4 analyses and discusses the results of the Eurobarometer data on the three dependent variables; section 5 provides the overall conclusions.

## **2. Theoretical framework**

### *2.1 the structural dimension of preferences for integration: neofunctional and postfunctional dynamics*

If “integration advances through crises”, as expected by historical institutionalists and theorists from all strands of functionalism, crises should affect preferences towards further integration. The original Neofunctional logic, as proposed by Haas (1958) implies that, as crises threaten the performance of institutions legitimated on the Output side (Scharpf, 1998), a preference would emerge towards further integration in order to re-establish the effectiveness of integrated policies and institutions. In other words, the leading reasoning in support of a Neofunctional interpretation of the crisis relies on the idea that, as the crisis sheds lights on the limited effectiveness of the existing institutions, such a failure of output legitimacy (Scharpf, 2009;2014) should create the required consensus for further integration. While the original Neofunctionalist setting concerned, in particular, the change in élites' preferences, later accounts (labelled as Neo-neofunctionalism- Schmitter, 1970; 2002) theorized that once integration were to “spill” into fiscal policies, a “transforming cycle” would emerge and mass-involvement in EU politics would begin (Schmitter 2002). The Neo-Nofunctional hypothesis, however, is matched by a post-functional hypothesis derived by the seminal contribution of Hooghe and Marks (2009). According to the Postfunctional account, resurging national identities would undermine the already limited input-legitimacy of the process of integration; which would then rely entirely on output legitimation; Thus a particularly powerful crisis – undermining output legitimacy and requiring further pooling of core powers of sovereignty to be addressed— would constrain, instead of strengthen, preferences towards integration. The fundamental

cleavage thus concerns the “sign” of this politicization process in front of a crisis: on the one hand popular opposition to further integration would emerge; on the other hand, it would sign the beginning of the involvement of mass-politics into the process of European Integration. The Eurocrisis, in particular, is a suited candidate to initiate a “transforming cycle”, provided that the new areas of integration touch upon economic and fiscal issues, key elements of the democratic process domestically. However, whether further integration, albeit being planned (Five Presidents Report, 2015), will actually be implemented is still an open question.

As suggested by Wijsman (2016), as the EU lacks effectiveness, it lacks sufficient output legitimacy; lacking output legitimacy, citizens are unwilling to transfer additional powers; but without additional powers, effectiveness (and therefore output legitimacy) remains out of reach. In fact, the nature of the expected integration is deemed to affect preferences on a systemic level: integration of redistributive policies without appropriate democratic procedures and/or without sufficiently developed common identity is likely to be opposed by citizens, generating a paralysis (Nicoli, 2015). This “circular illness” can be addressed only by integration of policies for which popular consent through referenda is not needed. Under this neo-neo functional hypothesis (Schmitter, 2002) we may expect an increase in preferences for integration following the crisis, but, simultaneously, a growing opposition against measures with redistributive implications.

## *2.2. the individual dimension of preferences for integration: identity versus self-interest*

Much of the current literature, instead of focusing on the broad effects of crises on preferences, anchors the study of preferences for integration into individual (rather than structural) phenomena. Emphasis is put on two particular processes: on the one hand, the degree of “nationalism” of the individuals; on the other, economic self-interest. The fundamental logic of rational choices approaches is that either citizens support European integration because they experience or expect material gains (losses) from integration, or because their sense of belonging to a particular community (or their understanding of their identity) alter their utility functions by adding a non-material compensation that makes up for the deviation from the choice that would maximise material gains.

Several studies find a prominent role for non-material factors relating to status, identity and community affiliations (Hooghe, 2003; Hooghe and Marks, 2005; McLaren, 2006; Betchel et al, 2014). In particular Betchel et al. (2014) explore how attitudes towards redistribution, socialization and political partisanship affected the German public opinion towards bail-out programmes; they find that group identity and cosmopolitanism, rather than individual perceptions about costs and benefits, are the real drivers of the attitude towards bailouts. Other studies stress the actual and expected costs and benefits of integration on their effect on preferences (Gabel and Palmer, 1995; Gabel, 1998 Kuhn and Stoeckel, 2014). A common problem with this setting, however, is that identity and economics are assumed to be reciprocally independent. However, economic factors contribute, in some extent to shape individual identities, both directly (as individuals tend to identify with values and communities that bring them direct advantage) and indirectly (through socialization processes). In other words, from a rational-choice perspective, individuals may support further integration because they enjoy material gains from it, or because they identify with it; but the latter is partially endogenous to the former. The embeddedness of self-interest and economic factors into self-identification variables limits the explanatory power of setting based on purely individual responses.

Whether grounding in self-interest or in identities the source of attitudes towards Europe, literature on preferences is also entangled with the body of work exploring the origins of Euroscepticism; a considerable amount of work has been done, at this regard, to understand the effect of the crisis on citizens' attitudes towards Europe (for instance Serricchio et al. 2013) and on the support for hard-line Eurosceptic parties (Hernandez and Kriesi, 2015; Nicoli 2016b). More broadly, many have used Eurobarometer data to explain the effect of the crisis on "support for the European Union" (for instance Armingeon and Ceka, 2014). However, trust in the EU, overall attitudes towards Europe, and the general self-understanding of citizens as "European", constitute differentiated concept from "preferences" for further integration in the economic governance, which constitute a more specific and technical issue<sup>1</sup>. Three main studies deal with the impact of the crisis on preferences for economic integration. First, Betchel et al. (2014) study the evolution of

---

<sup>1</sup> This may, indeed, give the rise to problems of external validity, as citizens may not be aware of what a specific measure of integration entails. However, provided that a "don't know" option is present in the survey, it is safe to assume that respondents have at least a generalized idea of what the measure in question implies

attitudes towards bail-outs in Germany, stressing the role of group identity and cosmopolitanism. However, their work is geographically delimited to Germany (and thus unable to catch the possible effects on the “losers” of integration); moreover, they tend to inflate their results by claiming that attitudes towards one-off, bail-out programmes hint to more general preferences in favour of more/less international redistribution (which, however, is not quite what bail-outs programmes and funds like the European Stability Mechanism are about). More specifically concerning the impact of the crisis for preferences for further integration is the work done by Kuhn and Stoeckel (2014). However, their study—being grounded in a single Eurobarometer wave conducted in late 2011—lacks the temporal depth required for a full understanding of how the crisis affected preferences over time. The same limitation applies to the competing study of Daniele and Geys (2015), which also relies on the 2011 Eurobarometer to assess preferences for fiscal integration. On a similar page, but in a different context, Hobolt (2014) finds evidence that core countries tend to have a structural preference in favour of further integration. Against this background, the paper aims to explore whether a neo-functional or a post-functional interpretation of the impact of the crisis on preferences for further integration is more appropriate.

### 2.3. *working hypotheses*

Building on the surveyed literature, this paper aims to fill a gap in current scholarship. The model should investigate (1) the effects of the Eurocrisis (in its different components) on preferences for further economic integration; adopting (2) a multi-year approach, thus enabling a dynamic understanding of the crisis; (3) providing insights that could shed light on the structural processes of European integration, thus providing empirical evidence towards either “grand” theory of integration.

In order to do so, we put forward several hypotheses. The baseline hypothesis (H.1) is the Neo-neofunctional proposition according to which the crisis increases the preference for further integration. According with H.1, we expect that the intensity of the crisis *increases* the demand for further integration in the governance sphere. The baseline hypothesis is contrasted with the pure Postfunctional hypothesis (H.2) according to which the “failure of output legitimacy” implied by the crisis reduces preferences for further integration. In line with H.2, we expect that higher levels of crisis are matched with lower preferences for integration; especially when economic data are matched with identity data.

Finally, a mixed hypothesis, more in line with Schmitter's concept of "transforming cycle, is drafted by combining a functional and a Postfunctional reasoning (h.3): following H.3, an economic downturn domestically would correlate with higher preferences for integration (in line with Neo-neofunctionalist logic); however, this general effect is expected to be moderated by those elements of the crisis which increase divide and polarization across the Union, contrasting different economic identities. In that instance, a Postfunctional reaction takes place as citizens of a given country would perceive further integration against their own interests and economic identity, thereby increasing polarization (in line with a Postfunctionalist logic). the expectation (h.3.1) is that, when the discussed form of integration requires mutualisation of financial resources (such as Eurobonds), the *negative reaction to bad performance abroad would be stronger*; similarly, (h.3.2), when the discussed form of integration concerns additional regulation or control (such as in the Governance index) *a bad performance abroad would in fact strengthen preferences for integration* as citizens tend to prefer solutions minimizing contagion to their countries.

### **3. Methodology**

#### *3.1 Operationalisation*

Operationalisation is, to some extent, limited by data availability and structure. A rational-choice approach to study of preferences would require data at individual level. While Eurobarometer does provide data on individuals and it is routinely used for comprehensive, cross-sectional studies on preferences towards integration (see, for instance, Hobolt 2014), investigating the effects of the crisis requires a time dimension which is not currently available at individual level. A second-best solution, which however spoils the opportunity of testing classical rational choice hypotheses on individual conditions, is to compute national averages over time; the effect of the crisis, instead of being apparent on the individual level, is approximated by nation-wide macro data. However, adding a time dimension generates issues in terms of Dependent Variables (DVs) selection: a comprehensive approach grounded on multi-component "governance index", as adopted by Kuhn and Stoeckel (2014), is possible only if the time-component of the Eurocrisis is not included. In fact, the several Eurobarometer time series upon which the governance index is built are not

reproduced with sufficient frequency to allow for the upgrading of the dataset into a full-fledged panel.<sup>2</sup> The first indicator is thus derived by the data series on preferences concerning Eurobonds, the only question of interest asked coherently throughout the entire period. A second indicator could be built by combining data on preferences for Eurozone Economic Policy Coordination (covering years 2011-2013) and on preferences for the creation of a Eurozone Financial Minister with powers of approval on national budgets (covering years 2013-2014). Finally, a broader question concerns whether the EU has sufficient powers to address the crisis.

### 3.2. *Dependent variables*

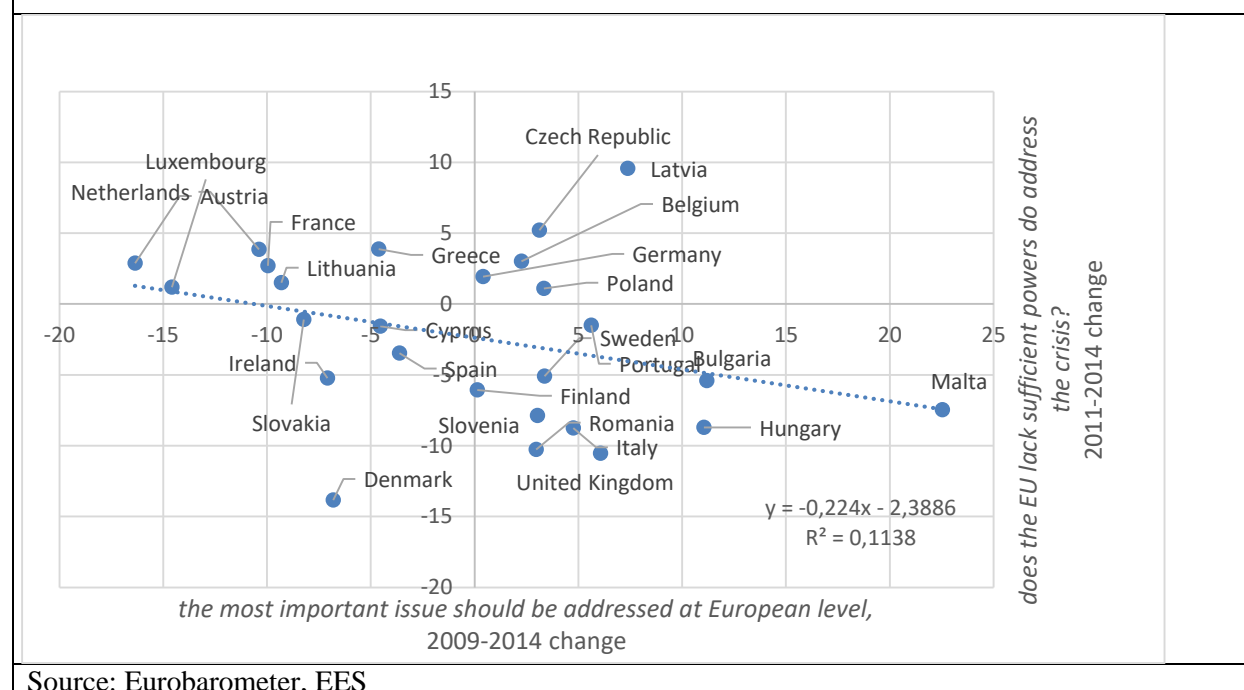
Against this background, a series of three separate regressions with different DVs is run.

The first DV (DV-1) is given national average of *negative answers* to the fifth question, “does the EU have sufficient powers to address the crisis”. The weighted European average of the respondents reporting that the EU lacks sufficient powers to deal with the crisis evolved only slightly over time, from 29% in early 2012 to 25% in early 2015; the standard deviation across European countries, however, decreased from 11 to 9, suggesting a general convergence of opinions. The interpretation of this answer is, however, controversial: a negative answer (the EU does not have sufficient powers to address the crisis) may indicate both that the EU, therefore, needs more powers, may indicate both that the EU, therefore, needs more powers, or that the crisis should not be addressed at EU level. Indeed, both sentiments seem to coexist, as shown in figure 1. On the vertical axis, figure 1 recalls the change, between 2011 and 2014, in the percentage of the population in each member country believing that the EU lacks sufficient powers to address the Eurocrisis; data are obtained from Eurobarometer.

---

<sup>2</sup> Annex 1 reconstructs, semester after semester, the availability of data on questions related to preferences concerning the economic crisis in the Eurobarometer.

Figure 1  
Integration Preferences and Powers Assessment



Source: Eurobarometer, EES

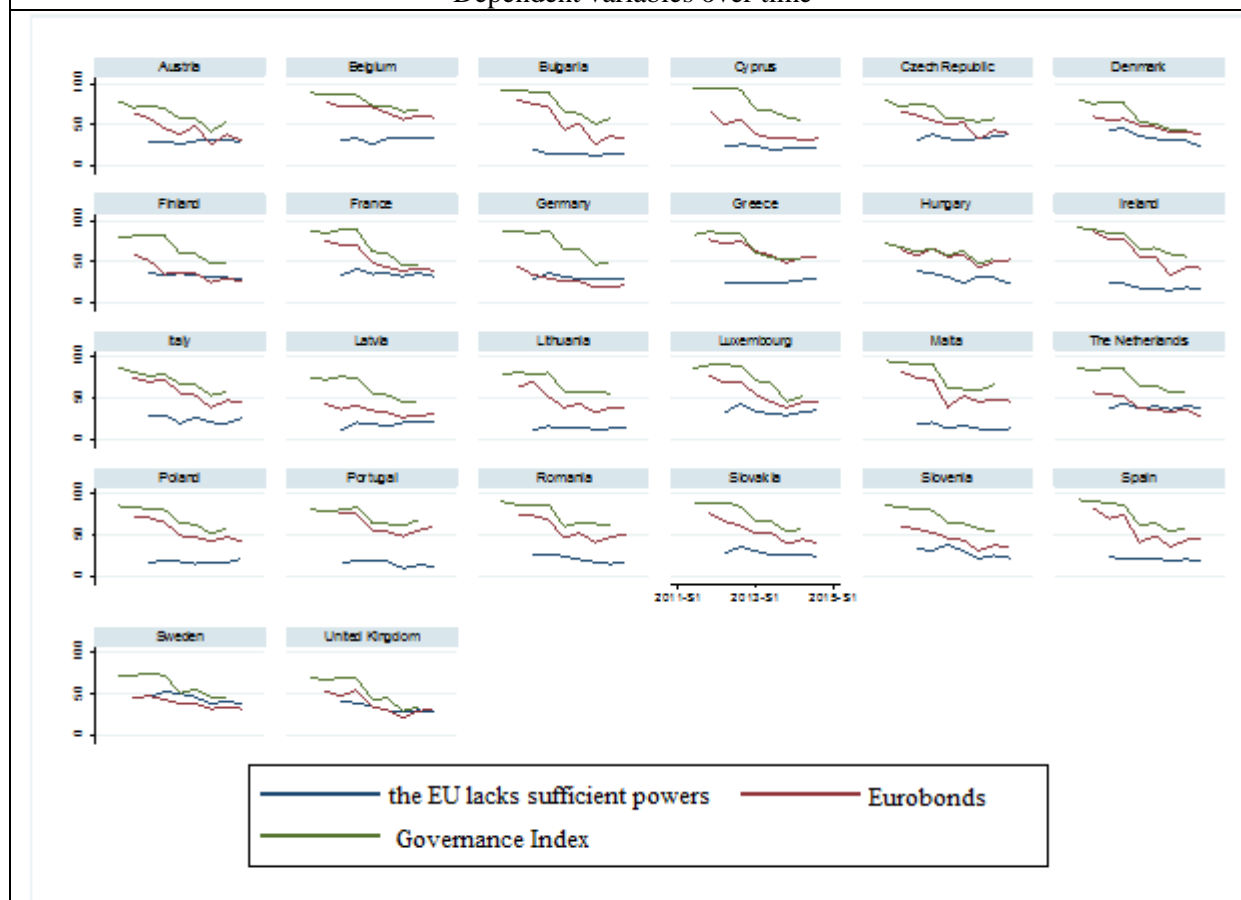
The horizontal axis reports the change (between 2009 and 2014) in the share of the population reporting that it would prefer to see the most important issue (for them) to be dealt with at the European level; data are obtained from the European Electoral Survey database (Egmond et al., 2013; Hermann et al., 2015).

Despite such a heterogeneous distribution of preferences, it is worth exploring the effects of the crisis as it captures the general mood towards the readiness and appropriateness of the European Union to tackle the Eurocrisis. The second DV (DV-2) concerns the specific preference for Eurobonds, for which data are available through almost the full time series. Finally, the third DV (DV-3) is built by combining data on preferences for Eurozone Economic Policy Coordination and for the Creation of a Financial Minister. Together, the two data-series cover the full period from 2011 to 2014; for the year 2013, characterised by an overlap, the average of national averages is taken. Table 1 reconstructs the availability, for each wave of Eurobarometer, of the required data. For all three DVs, figure 2 presents the evolution over time, country by country. It is worth noting that, at first glance, the trend is shaped downwards, suggesting a cooling of preferences for integration; however, the intensity of the Eurocrisis has also decreased since its heights in 2012.

Table 1  
Eurobarometer: data availability, preferences for integration

Euro-barometer code	Semester	Year	Preference for Eurobonds	Preference for Economic Policy Coordination	Preference for Economic Policy Coordination (Eurozone Only)	Preference for EU budgets approval	Does the EU have sufficient powers do address the crisis?
84.3	2	2015	▼	-	-	-	▼
83.3	1	2015	▼	-	-	-	▼
82.3	2	2014	▼	-	-	▼	▼
81.4	1	2014	▼	-	-	▼	▼
80.1	2	2013	▼	▼	▼	▼	▼
79.3	1	2013	▼	▼	▼	▼	▼
78.1	2	2012	▼	▼	▼	-	▼
77.3	1	2012	▼	▼	▼	-	▼
76.3	2	2011	▼	▼	▼	-	-
75.3	1	2011	-	-	▼	-	-

Figure 2  
Dependent variables over time



Source: own elaboration on Eurobarometer data series (2011-2015)



Table 2 Variables' lists		
<i>Variable Name</i>	<i>Description</i>	<i>Data source</i>
<b><i>Dependent Variables</i></b>		
<i>Lack of sufficient powers (DV_1)</i>	Share of “strongly disagree” and “fairly disagree” answers to the question “do you agree with the statement that the EU has sufficient powers to address the crisis?”	<i>Eurobarometer (2010-2015)</i>
<i>Eurobonds (DV_2)</i>	Share of “strongly effective” and “fairly effective” answers to the question “do you think that Eurobonds would be effective in tackling the crisis”?	<i>Eurobarometer (2010-2015)</i>
<i>Governance Index (DV_3)</i>	Average share of “strongly effective” and “fairly effective” answers to the questions “do you think that stronger coordination of the EMU countries would be effective in tackling the crisis”?, “do you think that an European Finance Minister would be effective in tackling the crisis”?, and “do you think that European approval of national budgets would be effective in tackling the crisis”?	<i>Eurobarometer (2010-2015)</i>
<b><i>Independent Variables</i></b>		
EuroArea	The country is member of the Eurozone	European Commission
Precrisis EuroArea	The Country was already member of the Eurozone prior to the crisis	European Commission
Growth Rate	The growth rate in the survey's semester	Eurostat
Crisis Index	Score on the Crisis indicator in the survey's semester	Nicoli, F. (2016a)
crisisBaseline	Pre-crisis score on the Crisis indicator	Nicoli, F. (2016a)
Greek Crisis	Dummy variable for the first semester 2015	
unemployment	The unemployment level in the survey's semester	Eurostat
Interest rate	Average yield on the 10-years public bond in the survey's semester	ECB
Fiscal balance	Fiscal surplus/deficit in the year of the survey	Eurostat
Banking Union Index	Progress index of Banking Union	Nicoli, F. (2016a)
Fiscal Union Index	Progress index of Fiscal Union	Nicoli, F. (2016a)
EU Integration index	ECB EU integration index, standardized	Dorucci et al.,(2015)
Core country	Core Eurozone countries: Austria, Benelux, Germany, France.	n/a
Nordic country	Nordic country: Baltics, Denmark, Sweden, Finland	n/a
New country	New country (2004 & 2007 enlargements)	
smallcountry	The country has less than 2 million citizens	Eurostat
Programme country	The country has been subject to an economic adjustment programme in the framework of the Eurocrisis	ECB
debt	Level of public debt in the survey's year	Eurostat
Eudebt	Average EU debt in the survey's year	Eurostat
Debt differential	Differential between domestic and EU debt level in the survey's year	Eurostat
Systemic Risk Index	ECB Composite Index for Systemic Stress	Holló et al. (2012-2016)
Nationalism	“only national” and “more national than European” answers to the Eurobarometer question “how do you see yourself in the near future”	Eurobarometer (2010-2015)
Semester	Whether the survey has been conducted in the Autumn (0) or Spring (1) semester	Eurobarometer

The independent variables (IVs) are selected to capture the multi-dimensional nature of the Eurocrisis. The ECB's Composite Indicator of Systemic Stress (CISS) originally developed by Holló et al. (2012) is included to capture the diffused financial dimension of the crisis. Moreover, the Crisis Intensity Index, which provides a multidimensional analysis of the Eurocrisis based on interest rate and Euroscepticism, is obtained from Nicoli Chapter 3- (Nicoli 2016b). Alternative measures on crisis intensity include growth rate, debt accumulation, differentials in debt levels from the European average; unemployment rate and interest rate, the two components of the Crisis Intensity Index, are also included individually.

At this regard, h.1 assumes that, overall, the impact of the crisis variables shapes upwards preferences for integration: the more intense is the crisis and the worse is domestic economic performance, the higher are preferences for integration; h.2, on the contrary, expects a negative reaction to the crisis. Finally, h.3 assumes that bad performance abroad, especially in terms of debt performance, would correlate with lower preferences for integration in the countries faring comparatively better. Control variables include the country size, the regional distribution, membership of the Monetary Union, and the progress achieved in European integration during the period under scrutiny; the latter is assessed through several variables: first, a standardized version of the Index of Regional Economic Integration of the ECB (Dorucci et al., 2015); second, through a set of dummy variables which capture the entrance into force of key decisions on fiscal and financial governance. Table 2 provides a list of all the IVs included in the several models run in this study.

### *3.4 The model(s)*

The strongly balanced panel is composed of 182 observations for DV-1, covering 26 countries (the EU28 minus Croatia and Estonia, for which data on interest rate on public debt are not available) from the first semester of 2012 to the first semester of 2015. The DV-2 also includes 182 observations, from the second semester of 2011 to the second semester of 2014. Finally, the DV-3 features 208 observations covering the full period from Autumn 2011 to Spring 2015. Although the panel structure of the data provides additional information in respect to previous analysis carried out by Kuhn and Stoeckel (2014) and Daniele and Geys

(2015), it also requires additional constraints in term of modelling choices. Three main alternative approaches can be used when looking at panel data: fixed effects, random-effects and pooled OLS. A fourth possibility is the Hausman-Taylor endogenous variables regression, which combines fixed effects and random effects.

As time-invariant known factors may play an important role in shaping preferences for further integration, the primary choice would be constituted by a random-effects model, provided that the robust version of the Hausman test is passed, therefore not violating the hypothesis that panel-specific errors are not correlated with the IVs. It follows that, for each of the 3 DVs, results are reported for random-effects models when consisted with the Robust version of the Hausman test; fixed effects, or -if appropriate- Hausman-Talyor results are reported otherwise.

For all three DVs, we are interested in the specific effect of the IVs capturing the effect of the crisis (1): *Growth Rate*, *EUdebt*, *debt\_differential*, *Unemployment*, *interest\_rate*, *deficit*, *crisis index*, and *Systemic Risk Index*. At this regard, the baseline Neofunctional hypothesis is that the higher the crisis intensity, the stronger the preference for further integration. Moreover, we are also interested in the possible effects of already-pursued integration (2): *integration\_index* attempts to capture the evolving nature of European integration in times of crisis. Also, we expect, we expect to have a negative coefficient for the various measures of already-achieved integration, capturing, to some extent, an “integration fatigue”.

However, an interaction term between the level of integration (captured by an index) and crisis intensity is also included, so it is the interaction between crisis intensity and the reported feeling of nationalism; we expect the first to be positively correlated with preferences for integration, as it suggests that existing integration has been not sufficient in addressing the crisis. Finally, a set of controls (3) is added, including *Euro Area* and *precrisis Euro area* membership, *programme country*, *Southern country*, *new member state*, *core member state* and *Nordic country*. We don't have particular expectations for most controls, with the exception of *Euro Area*, which we expect to be positively correlated with preferences for integration, and *programme country*, which we expect to be negatively correlated.

#### 4. Results

#### *4.1 Does the EU have sufficient powers to address the crisis?*

The first set of regressions concerned the DV-1: the share of respondents, in each country, that –between 2012 and 2015— believed that the EU lacked sufficient powers to address the crisis. The DV is the share of respondents that “strongly agree” and “fairly agree” with the statement. five different specifications (A1-A5) were tested. Specifications A1 only features the very basic components of the model, in order to focus on the effect of the growth rate. In A1, the crisis effect is captured by the yearly growth rate of the economy and by the differentials in the national debt burden from the European average, as well as by the crisis intensity index (Nicoli 2016a) and the ECB Systemic Risk Index (derived from Holló et al. 2012); A4 is included to allow comparison across DVs, as discussed in section 4.5. A5 includes the measure of “nationalism” derived from Eurobarometer.<sup>3</sup> Specifications A2 and A3 provide a wider selection of indicators of crisis intensity and interaction effects. In particular, specification A2 features unemployment and interest rate data, as well as a series of interactions; specification A3 includes the crisis intensity index and the ECB measure of institutional build-up, and their interactions. Finally, model A4 is included as a comparative term. At this regard, random-effects are consistent with the results of the robust Hausman test for all specifications, and therefore only random-effects estimates are reported (Table 3). Broadly, the effects of the crisis on the DV-1 seem to support the Neo-functional hypothesis, the stronger the hit of the financial crisis, the higher the share of the population believing that the EU lacks powers to address it. Even if nationalism plays a role, the effect of the crisis offsets the effect of nationalism.

More in detail, the Economy’s growth rate is statistically significant in specifications A1-A2, but fails to be significant in A3-A5. As expected, its sign is negative, suggesting that when the economy performs better, the sentiment that the EU lacks powers to address the crisis wanes. Unemployment measures, however, fail to be statistically significant in all the specifications where it is present directly (A2 & A3). The systemic risk index of the ECB is statistically significant only when nationalism is accounted for (A5)

---

<sup>3</sup> Accounted as the share of respondents reporting the answer “only National” and “national and European” to the question “how do you see yourself in the near future” (the alternative being “National and European, European and National, only European”). However, as the data series have been discontinued, including this variable implies a drop in N from 182 to 130 observations.

and strongly correlated, as expected, with perceptions of EU's weakness. The Crisis Index is significant in A3 (with a negative coefficient)..

Table 2  
Does the EU lacks sufficient powers?

	A1 (re)	A2 (re)	A3 (re)	A4 (re) (comparative)	A5 (re) (identity)
<b>precrisis EuroArea</b>	-1.326 (0.39)	<b>-13.753</b> <b>(3.01)***</b>	-1.387 (0.37)	1.400 (0.44)	0.436 (0.16)
<b>Growth rate</b>	<b>-0.529</b> <b>(2.13)**</b>	<b>-1.046</b> <b>(1.72)*</b>	-0.911 (1.31)	-0.255 (0.76)	-0.120 (0.43)
<b>Debt differential</b>	-0.030 (0.49)	<b>-0.104</b> <b>(1.65)*</b>	<b>-0.104</b> <b>(2.03)**</b>	-0.066 (1.26)	<b>-0.116</b> <b>(2.24)**</b>
<b>Small country</b>	<b>-7.949</b> <b>(2.51)**</b>	<b>-7.362</b> <b>(2.71)***</b>	<b>-9.183</b> <b>(3.03)***</b>	<b>-10.675</b> <b>(3.46)***</b>	<b>-9.370</b> <b>(3.21)***</b>
<b>Systemic risk index</b>	-1.414 (0.34)				<b>26.140</b> <b>(2.16)**</b>
<b>Crisis index</b>	-0.412 (1.19)		<b>-1.738</b> <b>(2.96)***</b>		
<b>crisisBaseline</b>	-0.939 (0.69)	-1.733 (1.16)	-1.317 (0.93)	<b>-3565</b> <b>(3.01)***</b>	
Nordic state	3.523 (1.02)	1.979 (0.56)	2.216 (0.64)		3.116 (0.88)
<b>Core state</b>	4.846 (1.61)	<b>6.214</b> <b>(2.55)**</b>	<b>4.668</b> <b>(1.73)*</b>		<b>6.603</b> <b>(2.52)**</b>
<b>Programme country</b>	-4.902 (1.12)	<b>-10.627</b> <b>(2.98)***</b>	<b>-6.349</b> <b>(1.65)*</b>		<b>-7.142</b> <b>(2.25)**</b>
<b>New member state</b>	-5.207 (1.35)	<b>-6.462</b> <b>(1.87)*</b>	<b>-7.256</b> <b>(2.08)**</b>		<b>-9.005</b> <b>(2.78)***</b>
<b>fiscal balance</b>	-0.363 (1.48)	-0.359 (1.49)	<b>-0.385</b> <b>(1.83)*</b>	-0.266 (1.10)	-0.101 (0.28)
<b>Eudebt</b>	<b>-1.198</b> <b>(3.78)***</b>	<b>-1.362</b> <b>(5.16)***</b>	<b>-1.133</b> <b>(4.08)***</b>	<b>-0.879</b> <b>(3.86)***</b>	-0.498 (1.38)
unemployment		-0.596 (1.63)			
high_unemployment		0.184 (1.24)	-0.054 (0.28)		
interest rate		-0.200 (1.22)			
<b>precrisisEuroArea*unemployment</b>		<b>1.302</b> <b>(2.44)**</b>			
<b>integration index</b>			<b>-140.010</b> <b>(1.86)*</b>		
<b>integration*crisis</b>			<b>26.713</b> <b>(2.69)***</b>		
precrisisEuroArea*growth		0.832 (1.28)	0.501 (0.71)		
<b>Nationalism</b>					<b>-10.944</b> <b>(2.17)**</b>
<b>nationalism*crisis</b>					<b>1.601</b> <b>(2.26)**</b>
_cons	<b>139.451</b> <b>(4.68)***</b>	<b>160.674</b> <b>(6.23)***</b>	<b>142.758</b> <b>(5.42)***</b>	<b>143.925</b> <b>(4.02)***</b>	<b>74.027</b> <b>(2.53)**</b>
N	182	182	182	182	130
Robust Hausman	<b>passed</b>	<b>passed</b>	<b>passed</b>	<b>Passed</b>	<b>passed</b>

Counter-intuitively it suggests that higher interest rates and unemployment (indicative of a stronger crisis) are associated with lower shares of the population believing that the EU lacks sufficient powers to address the crisis. Likely however the negative effect is due to the presence, in the specification, of the index of EU integration (strongly negatively correlated with the DV) which – increasing over time without solving the crisis- absorbs most of the perceptions of powerlessness of the EU. Also, it is worth noting that, in the period under consideration (2012-2015) only very few countries experienced substantially high interest rates (namely Portugal, Greece and Cyprus). Already from the second half of 2012, the entrance into force of the OMT curved down interest rates in all but the most troubled countries. Furthermore, countries with very low interest rates, all belonging to the “core” group of the Eurozone and the Nordic countries, may have perceived the OMT effects on rates as a source of moral hazard, undermining the reform effort in troubled countries. It remains clear, however, that countries experiencing strong distress from the crisis did not believe that the EU lacked powers to address it.

The differential of the domestic debt rate from the European average is negatively correlated and significant in 3 out of 5 specifications, suggesting that – as the growth rate of a country’s debt outpaces the EU’s average, the EU control becomes stricter, and therefore a smaller share of the population believes that the EU lacks powers: in turn, when a country manages to reduce its own debt in respect to the rest of the EU, the sentiment is that the EU does not have enough powers to replicate the same success abroad. Accordingly, the level of EU debt is always significant (except for A5) and negatively associated with the DV. In terms of integration, the integration index is strongly negatively correlated with the perception of lack of powers when included in specification A3; the interaction effect with the Crisis Index is also statistically significant and positively correlated: meaning that, in the countries where the crisis is more intense, the new procedures and institutions introduced since 2012 have been perceived as sufficient to address the crisis, but relatively less in the countries where the crisis was comparatively worse. Finally, the effect of introducing identity measures changes little in the results but adds perspective. The signs of the statistically-relevant variables remain broadly the same; nationalism, as expected, is strongly negatively correlated with the idea that EU lacks further powers; however, its interaction with the crisis index is positive, suggesting that the stronger the crisis, the weaker it becomes the nationalistic-fuelled sentiment that the EU has sufficient powers.

### *4.3 Preference for Eurobonds*

The second DV concerns the preference for the creation of Eurobonds. This particular question is the only one featuring in each Eurobarometer from the second half of 2011 to 2015, indicating a persistent interest of the European Commission and of the European Parliament in the matter. Not differently from the previous cases, several different specifications have been tested (Table 4).

Specification B1 reports the growth rate and the Systemic Risk Index measures of the crisis; specification B2 and B4 add the Crisis Intensity Index, controlling for the different starting levels and for countries object of an economic adjustment programme; the latter excludes regional controls; Specification B4 includes a long series of interactive terms for the Eurozone membership; B5 is included to allow for comparison across DVs, and B6 introduces data on nationalism from Eurobarometer. In specifications B1-B3, the independence hypothesis held and therefore random-effects estimates are reported; in specification B4 however, the model failed to pass the robust version of the Hausman test, and therefore fixed-effects estimates are reported.

Overall, preferences for Eurobonds seem to depend primarily on the general (European-wide) perception of living through particularly strong crisis times (the Systemic Risk Index; the 2015 Greek crisis episode), with a second component depending on domestic performance (positive performance tends to decrease the sentiment for debt mutualisation); finally, the total level of European debt acts as a moderator to these effects.

More in detail the growth rate is negatively correlated and statistically significant in 4 specifications, suggesting that the better the domestic economy performs, the weaker is the perception that the EU needs to mutualize debt, therefore supporting h.1. Such an explanation is complemented by the ECB's Systemic Risk Index, that is significant and positively correlated to the DV. The Neofunctional explanation is somehow moderated by the estimations on the effect of the EU debt levels: the higher the European debt (always statically significant and negative), the lower the appetite for sharing the burden; together, they seem to support h.3.1 rather than h.1.

Table 3						
Powers, Governance, Eurobonds	Preferences for Eurobonds					186
	B1 (re)	B2 (re)	B3 (re)	B4 (fe)	B5 (re) (comparative)	B6 (re) (identity)
<b>Growth rate</b>	<b>-1.324</b>	<b>-1.385</b>	-1.402	<b>-1.109</b>	<b>-1.018</b>	-0.633
	(3.09)***	(3.09)***	(3.19)***	(2.46)**	(2.51)**	(1.10)
<b>EU debt</b>	<b>-4.333</b>	<b>-6.181</b>	<b>-6.191</b>	<b>-2.359</b>	<b>-3.722</b>	<b>-6.525</b>
	(9.13)***	(10.94)***	(11.72)***	(4.57)***	(9.02)***	(7.08)***
<b>Greekcrisis</b>	<b>-5.647</b>	<b>-8.672</b>	<b>-8.752</b>			<b>-9.070</b>
	(3.93)***	(6.49)***	(8.61)***			(4.89)***
<b>Programme country</b>	3.516	5.599	<b>7.459</b>			
	(0.66)	(1.26)	(1.89)*			
Fiscal balance	-0.012	-0.027			-0.124	
	(0.03)	(0.07)			(0.32)	
EuroArea	0.538	-0.653		-36.193		0.558
	(0.23)	(0.29)		(1.21)		(0.32)
<b>Nordic state</b>	<b>-11.512</b>	<b>-7.858</b>				
	(2.41)**	(2.02)**				
<b>Systemic risk index</b>	<b>14.514</b>					<b>34.042</b>
	(2.69)***					(1.85)*
debt	-0.040			-0.653		0.032
	(0.63)			(1.04)		(0.15)
small country	0.558				0.343	
	(0.09)				(0.06)	
Core state	-3.948					
	(0.53)					
New state	1.107					
	(0.25)					
<b>integration index</b>		<b>95.694</b>	<b>93.877</b>			
		(1.70)*	(1.66)*			
Crisis index		-0.416	-0.461			
		(0.73)	(0.81)			
<b>crisisBaseline</b>		<b>2.506</b>	<b>3.159</b>		<b>2.840</b>	
		(1.65)*	(2.35)**		(2.66)***	
Debt differential					-0.012	
					(0.19)	
Precrisis EuroArea					3.310	
					(0.79)	
<b>Nationalism</b>						8.476
						(1.18)
nationalism*crisis						-1.116
						(1.08)
unemployment				<b>-1.092</b>		
				(1.91)*		
interest rate				0.322		
				(0.26)		
<b>Fiscal Union Index</b>				<b>-4.750</b>		
				(5.07)***		
banking Union Index				-1.132		
				(1.23)		
Eur*unemployment				1.252		
				(1.27)		
Eur*interest				-0.415		
				(0.32)		
Eur*debt				0.570		
				(0.88)		
Semester					<b>-0.010</b>	
					(4.81)***	
_cons	<b>421.426</b>	<b>559.649</b>	<b>555.103</b>	<b>313.909</b>	<b>539.307</b>	<b>595.544</b>
	(9.99)***	(11.95)***	(12.68)***	(6.43)***	(13.98)***	(7.94)***
N	208	208	208	208	208	130
Robust Hausman	<b>Passed</b>	<b>Passed</b>	<b>Passed</b>	<i>Failed</i>	<b>Passed</b>	failed



The simple level of national debt is however not significant, nor it is the differential. The dummy identifying the 2015 Greek crisis episode (the long negotiations between the Greek government led by Syriza and the so-called Troika (EU, ECB, IMF) on the third bailout package in S1 2015), which suddenly reignited the Eurocrisis when it was broadly perceived as settled, is strongly negatively correlated, suggesting that the Tsipras' government hard-line stance to renegotiate better terms was not taken positively by Europeans. Economically distressed countries, however showed generally higher support for the proposal: the baseline value of the indicator (CrisisBaseline) is significant at 5%/10% level depending on the specification, and its positive coefficient suggests that countries struck earlier by the crisis have maintained their preference for fiscal integration. The additional elements of the crisis, such as the interest rate or the unemployment rate (specification B4) generally fail to be statistically significant, with the exception of unemployment at 10% level for specification B4. The same applies to several Euro Area interactions, suggesting that- concerning preference for Eurobonds- the crisis had no appreciably stronger effect on the Eurozone's public opinion. Data on identities return a mixed profile. Eurobarometer data series on nationalism, and its interactions with crisis measures, are not significant nor have an appreciable effect on other variables once introduced in the regression model (specification B6). Among the country group variables, only the dummy for the group of Nordic countries holds a statistically significant (and negative) coefficient, confirming the prior intuition that Nordic countries are not very much fond of the idea of debt mutualisation; which identified, which had widespread media diffusion.

#### *4.4 Governance Index*

The final DV tested in this study is a composite index of the answers to several different questions concerning stronger governance in the fiscal and macroeconomic field. The first question, covering the years from the first semester of 2011 to the second semester 2013 asked the respondents to assess how effective would be, in addressing the Eurocrisis, to introduce enhanced Eurozone coordination of fiscal and macroeconomic policies. The second question, present in Eurobarometer between the first semester of 2013 and the second semester of 2014, asked the respondents to assess how effective it would be to have the Union to approve the budgetary laws of member-states. Finally, the third question, present in the Eurobarometer only in 2013, required the respondents to assess the effectiveness of the creation of a

European Union's Finance Minister, proposed, among others, by the German finance minister W. Schauble (Böll and Von Hammerstein, 2012; Karagiannis and Guidi, 2014; Enderlein and Haas, 2015).

Table 4 governance index						
<i>Governance index</i>	C1 (re)	C2 (re)	C3 (re)	C4 (fe)	C5 (re) (comparative)	C6 (fe) (identity)
crisis Baseline	0.0147 (1.50)	<b>0.017</b> <b>(1.75)*</b>	<b>0.017</b> <b>(1.70)*</b>		<b>1.542</b> <b>(1.94)*</b>	
growthrate	<b>-0.0105</b> <b>(2.60)***</b>	<b>-0.004</b> <b>(1.82)*</b>	0.001 (0.14)	<b>-0.007</b> <b>(2.79)***</b>	<b>-0.729</b> <b>(3.62)***</b>	-0.006 (0.63)
smallcountry	<b>0.0522</b> <b>(2.20)**</b>	<b>0.035</b> (1.50)	0.033 (1.29)		2.995 (1.35)	
precrisis EuroArea	<b>0.0587</b> <b>(2.58)***</b>	<b>0.107</b> <b>(3.06)***</b>	<b>0.100</b> <b>(2.25)**</b>		<b>9.582</b> <b>(3.78)***</b>	
unemployment		-0.003 (1.92)*	-0.005 <b>(1.71)*</b>			
fiscal_balance		<b>-0.004</b> <b>(2.09)**</b>	<b>-0.004</b> <b>(1.94)*</b>	-0.003 (1.43)	<b>-0.278</b> <b>(1.66)*</b>	-0.001 (0.54)
debt differential		-0.001 (1.35)	-0.001 (1.45)	-0.001 (1.11)	<b>-0.093</b> <b>(2.62)***</b>	-0.000 (0.05)
<b>EU debt</b>		<b>-0.011</b> <b>(2.13)**</b>	<b>-0.011</b> <b>(1.96)**</b>	-0.007 (1.36)	-0.678 (1.60)	<b>-0.086</b> <b>(4.24)***</b>
new country		0.018 (0.62)	0.017 (0.60)			
core country		-0.010 (0.31)	-0.008 (0.24)			
Integration Index		<b>10.603</b> <b>(6.67)***</b>	<b>10.676</b> <b>(6.68)***</b>	<b>9.530</b> <b>(6.12)***</b>		
Systemic Stress Index				<b>0.199</b> <b>(6.31)***</b>		0.121 (0.85)
Semester		<b>-0.001</b> <b>(10.72)***</b>	<b>-0.001</b> <b>(10.58)***</b>	<b>-0.001</b> <b>(8.89)***</b>	<b>-0.025</b> <b>(8.85)***</b>	0.000 (0.57)
EUR*gdpGrowth			<b>-0.006</b> <b>(1.11)</b>			
EUR*unemployment			0.002 (0.71)			
Euro Area				<b>-0.041</b> <b>(2.20)**</b>		-0.027 (1.10)
Crisis Index				-0.008 (1.19)		<b>-0.025</b> <b>(2.35)**</b>
nationalism						0.108 <b>(1.89)*</b>
crisis*nationalism						<b>-0.016</b> <b>(1.98)*</b>
_cons	<b>58.255</b> <b>(10.91)***</b>	<b>12.077</b> <b>(11.89)***</b>	<b>12.173</b> <b>(11.84)***</b>	<b>10.752</b> <b>(9.70)***</b>	<b>587.020</b> <b>(21.33)***</b>	<b>7.700</b> <b>(5.47)***</b>
Robust Hausman N	<b>Passed</b> 208	<b>Passed</b> 208	<b>Passed</b> 208	<i>failed</i> 208	<b>Passed</b> 208	<i>failed</i> 130
* $p < 0.1$ ; ** $p < 0.05$ ; *** $p < 0.01$						

Similarly to DV-1 and DV-2 this variable is built on the average share of respondents responding to “fairly agree” and “strongly agree” with the effectiveness of each of the solutions. Of course, for the years 2011-

2012 DV-3 is equal to the answers to the first question, while for the year 2014, to the answers to the second question. For 2013, DV-3 is equal to the average share of positive replies over the three variables considered.

Six different specifications have been run. Specification C1 includes only the basic elements of the model: growth rate, country size and Euro Area membership. C2 includes additional elements of the crisis besides growth rate, such as unemployment, debt differentials, and deficit; it also includes the ECB's index of European integration and a full set of country controls; C3 interacts pre-crisis Euro membership with the crisis components (GDP and unemployment in particular). C4 includes the Crisis Intensity Index and the Systemic Stress Index instead of the unemployment rate and the interest rate. Again, C5 is included to allow comparison across DVs and C6 includes identity measures. The Robust Hausman test failed for specifications C4 and C6, so, fixed-effects estimates are reported instead of the usual random-effects.

The estimated effects of the explanatory variables are in line with the results of the previous two DVs. The growth rate is significant at 1% in specification C1, C4 and C5, and at 10% in C2, with a negative coefficient as expected: lower growth rates are generally associated with higher preferences for strengthened fiscal and economic governance. However, when interaction effects with Eurozone membership are included (C3) the statistical significance of the effect seems to fade. Against the straightforward neofunctionalist explanation, specifications C2 and C3 show that higher levels of unemployment are negatively correlated with the governance index (the higher the unemployment, the lower the preference for a constrained economic policy). The opposite applies to higher fiscal balance (the smaller the deficit, the less countries seem to be in favour of strengthened control). This seems to suggest that citizens favour European supervision of fiscal policy, but not when the country is troubled by high unemployment.<sup>4</sup> In other words, the effect may be explained by a diffused preference of citizens for the EU to keep their own domestic government on check; a preference, therefore, for the EU's "external constraint" (Panagiotarea, 2014). With almost no exceptions across specifications, Euro Area membership, and the degree of pre-crisis economic distress (*CrisisBaseline*), are positively correlated with preferences for stronger governance. The only

---

<sup>4</sup> This is confirmed by the positive coefficient and by the 1% statistical significance of the interaction between unemployment and fiscal balance, tested in a specification not presented in table 3 for succinctness

statistically significant and quantitatively large coefficient is attributed to the ECB's index of European Integration. At this regard, however, a word of caution is worth mentioning: as the Index tends to increase over time (with only a few episodes of reduction over the 60 years' timeline anyway not included in panel's time frame) it tends to equally capture a general effect of the "flowing time", and therefore may be biased as it may contain the effects of eventually omitted variables. Also, the size of the coefficient, appearing so large, can be misleading: being the index standardized (0-1), its actual values are extremely small, varying from a minimum of 0,04 to a maximum of 0,08.

#### 4.5. Comparative assessment

Table 6  
Comparative random effects estimates

	EU lacks sufficient powers (A2)	Eurobonds (B5)	Governance index (C5)
	<i>Random effects</i>	<i>Random effects</i>	<i>Random effects</i>
crisisBaseline	<b>-3.565</b> (3.01)***	<b>2.840</b> (2.66)***	<b>1.542</b> (1.94)*
growthrate	-0.255 (0.76)	<b>-1.018</b> (2.51)**	<b>-0.729</b> (3.62)***
smallcountry	<b>-10.675</b> (3.46)***	0.343 (0.06)	2.995 (1.35)
precrisisEuroArea	1.400 (0.44)	3.310 (0.79)	<b>9.582</b> (3.78)***
fiscal_balance	-0.266 (1.10)	-0.124 (0.32)	<b>-0.278</b> (1.66)*
debtdifferential	-0.066 (1.26)	-0.012 (0.19)	<b>-0.093</b> (2.62)***
Eudebt	<b>-0.879</b> (3.86)***	<b>-3.722</b> (9.02)***	-0.678 (1.60)
semester	-0.001 (0.68)	<b>-0.010</b> (4.81)***	<b>-0.025</b> (8.85)***
_cons	<b>143.925</b> (4.02)***	<b>539.307</b> (13.98)***	<b>587.020</b> (21.33)***
Robust Hausman	<b>Passed</b>	<b>Passed</b>	<b>passed</b>
N	182	208	208

\*  $p < 0.1$ ; \*\*  $p < 0.05$ ; \*\*\*  $p < 0.01$

Some variations exist across the different DVs. Table 6 reports the results for the reduced, comparative specification (A2, B5, C5). As noticeable, the main differences are between DV-1 and the other two DVs, although the signs of the coefficients tend to remain, broadly, the same. The most interesting difference is likely the divergent sign, across specifications, of the coefficient of *CrisisBaseline* (identifying the 2008

situation of unemployment and interest rates). While a higher *CrisisBaseline* indicator associates with stronger preferences for both Eurobonds and Governance, it also associates strongly with lower perception that the EU lacks sufficient powers. This seems to support the mixed functional/Neofunctional hypothesis, as countries are in favour of further integration when it suits their interests (Eurobonds, stronger governance) but not when they already perceive excessive involvement of the EU in their domestic matters.

## 5. Conclusions

Two key questions inspired this paper. On the empirical level, given the Brussels circles' appetite for further integration, the paper sought to investigate the real effects of economic performance, in times of crisis, on citizens' preferences for further integration. Conveniently, on a theoretical level, such an empirical answer may shed light on the interaction between the alleged Neofunctional dynamics of integration and the emergence of a Postfunctional dynamic of integration. The Neo-neofunctional dynamics of integration, driven by the need to re-establish the fading output legitimacy assumes that- when a crisis hits- preferences for integration tend to strengthen. Conversely, a Postfunctional integration dynamics implies that (i) democratic deficit becomes a driver of competences' allocation and that (ii) if a performance deficit is perceived, it would rather weaken preferences for further integration (Wijsman, 2016). At this regard, the Postfunctional hypothesis implies that crisis intensity and preferences for integration have a negative correlation. The baseline, Neofunctional hypothesis therefore assumed that crisis intensity and preferences for integration tend to be positively correlated; the Postfunctional hypothesis postulates, instead, that the correlation is negative.

Generally, the econometric results fail to confirm beyond doubt either h1 on Neofunctionalism, or h2 on Postfunctionalism. We observe a general tendency in favour of the mixed interpretation offered by h.3, albeit with many nuances, with a slightly stronger weight attributed to its Neofunctional component. The main crisis indicator – the economy's growth rate— clearly shows a strong and robust negative correlation with all three dependent variables, supporting the Neofunctional hypothesis. Other elements of the crisis, either considered together, such as within the Crisis Index, or separately, like debt, deficit, European debt and unemployment data, often fail to pass the significance threshold. When they succeed, they hold

contrasting results. Higher European debt levels, as well as higher unemployment, show a negative correlation with preferences, supporting instead a Postfunctional interpretation of the crisis.

However, further support for the Neofunctional interpretation is given by “soft” indicators of crisis intensity, such as the baseline level of crisis intensity (positively correlated with preferences for specific actions) and the dummy variables identifying countries under economic adjustment programmes. Moreover, if a Neofunctional effect of the crisis on preferences for integration exists, it appears to be differentiated between domestic effects and European effects: domestic under-performance associates with higher preferences for integration, while under-performance abroad tends to depress preferences. All in all, data on preferences are not sufficient in determining whether the crisis, at its heights, generated the conditions for further integration in a classical Neofunctional dynamics, and therefore the cooling of enthusiasm for further integration is due to the improving economic performance, or whether resentment for the EU failures in economic policy abroad translates, overall, in lower willingness for further transfer of competences.

Despite shedding lights on the impact of crisis intensity on the preferences for fiscal integration, however, the paper suffers from a major shortcoming, dictated by data availability. Lacking pre-2011 data on preferences for fiscal integration, the methodology here adopted is unable to show whether the crisis had induced an original “positive shock” in preferences, successively faded away once the effect of the crisis diminished, or whether pre-crisis preferences for fiscal integration were even higher. Unfortunately, in the absence of a longer, pre-crisis dataset, a final evaluation of the full effect of the crisis is not possible, although –as shown here – an assessment of the impact of crisis intensity is within reach.

.

## Chapter Seven: Hard-line Euroscepticism and the political fallout of the Eurocrisis: evidence from a 108 elections panel study

### **Abstract**

The 2014 European elections led to a sharp rise in the electoral consensus of parties and independent parliament members perceived as Eurosceptic. This paper analyses the interconnections between distressed economies and the electoral success of extreme Eurosceptic parties. On a panel of 108 elections between 2008 and 2015, the random-effects model shows the relative effect of long- and short-term political trust, economic performance indicators, and institutional variables in determining the rise of hard-line Eurosceptic parties. In contrast with previous studies, which have tended to de-emphasize the effect of economic performance in determining the success of Eurosceptic forces, the results of this paper detect both a direct and a mediated effect of the economic crisis on the electoral success of extreme Eurosceptic parties.

*Note* : a version of this paper is published on the *Journal of Common Market Studies*.





# The political fallout of the Eurocrisis: evidence from a 108 elections panel study

## 1. Introduction

The Eurocrisis has severely damaged the economic prosperity of many European Union countries. However, the extent to which it has contributed to the emergence of an existential risk for the Union itself is still matter of discussion. Extreme Eurosceptic parties embody such a threat: Did the Eurocrisis strengthen the hand of extreme Eurosceptic parties and, if yes, how much?

Since the French and Dutch rejections of the Constitutional Treaty in 2005, there has been a growing attention concerning the rise of Eurosceptic parties in the member states and the structural features of the European Union that might have triggered the change (Startin and Krouwel, 2013). However, Euroscepticism has regained primary political relevance only as of 2010; the nationalist parties traditionally opposing European integration have been flanked by new groups identifying the European governance and institutions as the leading political agents responsible for the resilience of the financial crisis in the Euro Area. The connection between the economic crisis and the legitimacy crisis is an issue of survival for the EU. As it stands today, the EU is often described as a political project legitimized by its performance and achievements rather than by the direct election of its leadership (Scharpf, 1970, 1999, 2009). The long duration of the European economic crisis may have provoked a fading of “output legitimacy” and a blossoming of contestation against the EU. The declining output legitimacy may result in two effects: On the one hand, mainstream

parties may become increasingly “soft Eurosceptic”; on the other hand, “hard-Eurosceptic” parties may enjoy an electoral boost. Whereas the change in the discourse of mainstream parties may weaken the capacity of the EU to introduce a further pooling of competences and resources, the rise of extreme Eurosceptic parties constitutes an existential threat for the Union itself. The 2014 European elections have indeed led to a sharp rise in EU opposition in parties and independent parliament members, although the political forces referred to as hard Eurosceptic often share no other ties than the common opposition to the European integration project.

However, the rise of anti-European sentiment that has emerged in the last few years should hardly surprise European Union scholars. Since the early days of the EU, a number of “grand theories of integration” have discussed the rise of anti-European sentiment as a byproduct of Europeanization. For instance, both early (for instance, Haas, 1958, 1964) and contemporary (for instance, Schmitter, 2002) versions of Neofunctionalism have incorporated the emergence of Euroscepticism as a possible outcome, in the form of the nationalist reaction to the progressive centralization of political power. In Haas’ own words, the return of nationalism is the natural consequence of the EU’s shift from the integration of *policies* to the integration of *polities* (Haas, 2003, introduction). Second, the classical party formation theory developed by sociologists Lipset and Rokkan (1967)<sup>59</sup> assumed that one of the first challenges faced by newborn states and political systems is the repartition of competences and redistributive power between the central and peripheral institutions; in this perspective, the shift of powers towards the centre cannot happen without politicization and contestation. Finally, the growing body of literature concerning the so-called “democratic deficit” of the European Union, particularly in Weiler (2000) and Majone (1997, 2013), discounts (for different reasons<sup>60</sup>) Euroscepticism as a possible byproduct of deepening integration.

Against this background, we are interested in understanding whether the crisis has played a role in shaping Eurosceptic consensus. We expect to observe that the Eurocrisis has strengthened consensus for extreme

---

<sup>59</sup> See also Flora, Kuhnle and Urwin (eds) (1999)

<sup>60</sup> For Weiler, Euroscepticism is the reaction to the attempt of deepening EU integration without the creation of a single demos. For Majone, Euroscepticism may emerge as a consequence of increased EU competences beyond its regulatory powers into fields of competence requiring input legitimacy.

Eurosceptic parties where the crisis has been more profound; the logic of this effect is discussed in section 2.3.

The existing quantitative literature on the issue has in part downplayed the role of the crisis in boosting Euroscepticism upwards; however, as our results show, and in contrast with previous studies, both unemployment and economic cycle variations appear to affect votes for Eurosceptic parties. The goal of this paper is thus to complement qualitative research and country-by-country empirical research by offering a European-wide quantitative analysis, which is today limited to a small number of recent publications. The paper adopts panel-data analysis on a custom database of 108 elections in 27 EU member states<sup>61</sup> from 2008 to 2015, with the aim to better understand the causes of the emergence of electoral Euroscepticism.

The paper is organized as follows. Section 2 discusses the notion of Euroscepticism and collects literature on Euroscepticism and the crisis. Section 3 presents the methodology and the data. Section 4 discusses the results of the first panel regression, looking at the determinants of Euroscepticism. Finally, section 5 presents the conclusions, limitations and implications of our results.

## **2. The dimensions of Euroscepticism**

Euroscepticism, more than a political ideology, can be considered a loose label under which a variety of forms of opposition to the EU can be collected. As Harmsen and Spiering (2004) note, the original phenomena of Euroscepticism (dating from before the creation of the European Union in 1992) can be basically divided in two main streams: first, a wide opposition to the very concept of European political integration, which particularly characterizes the British political forces and far-right political groups in the member states; second, a particular opposition to certain policies of the European Communities, such as trade liberalization or the prohibition of state aid. This second version of opposition to European integration characterized mainly the socialist political family across Europe, which considered the European-driven

---

<sup>61</sup> Croatia was not part of the EU during the crisis, so it is not included in the study.

market liberalization a danger for social democracies and welfare-state expenditure programmes. This form of Euroscepticism gained support particularly in France and in the Nordic countries. In sum, Euroscepticism can be studied along two dimensions: a “hard” versus “soft” cleavage and an “electoral” versus “attitudinal” dimension. The next paragraphs discuss the benefits and drawbacks of each approach.

### *2.1 Soft versus hard Euroscepticism*

Although the political families opposing European integration have evolved over time, the distinction between “hard Euroscepticism” (opposition to the EU) and “soft Euroscepticism” (opposition to a subset of EU policies, to a particular political direction of the EU) proposed by Taggart and Szczerbiak (2002) remains a powerful key to understanding the phenomenon. Whereas the definition of “hard” Euroscepticism is straightforward, it remains unclear how to precisely evaluate the extent of “soft” Euroscepticism. The distinction between calling for a substantial overhaul of European integration and the opposition to the current institutional setting of policies is fairly weak: Euro-reformists and Euro-federalists could, in principle, be labelled as “soft Eurosceptic” to the extent that they oppose the current form of European Integration. To address this issue, Taggart and Szczerbiak (2008) discuss how to distinguish soft-Eurosceptic areas into “critics” and “sceptics”, but they do not propose a fully convincing methodology. Moreover, when looking at parties rather than attitudes, there are compelling reasons to focus on the “hard” dimension:

- 1) *The increased politicization of the EU.* Most parties have embodied a certain degree of critique of the EU; it has become common practice among national parties to adopt specific reform plans and agendas *vis-à-vis* the European Union, justifying a range of criticism towards the EU itself and some of its policies (Nicoli, 2014). The very process of the politicization of the EU is partly responsible for this effect: As the direction of the European Union increasingly becomes a matter of political debate and electoral decision making, a degree of discussion and eventually criticism becomes unavoidable. The institutionalization of the main policies of the EU within the treaties

implies, to a certain extent, that criticism of the policies is *also* criticism of the system itself. As partial criticism of the EU has become widespread even across mainstream parties, the category of “soft Euroscepticism” has lost a large part of its explanatory power.

- 2) *Government-opposition dynamics*: Many EU-brokered policies, since the crisis, have been introduced through inter-governmental meetings and/or European Commission recommendations or memoranda of understandings with international lending institutions. In both cases, governments have to implement the agreed legislation: It follows that soft Euroscepticism may become a trait of mainstream opposition parties, and thus, a more precise measure of Euroscepticism is needed.

This study focuses mainly on extreme forms of Euroscepticism, i.e., those political parties and movements actively calling for a reduction of EU competences, if not for a simple dismantlement of the institutions. Other classifications of Euroscepticism have been proposed by scholars. In particular, the dichotomy between “diffuse opposition” (opposition to the European project and its values) and “specific opposition” (opposition to the specific forms of European integration in a given moment) proposed by Wessels (2007) recalls the “soft” versus “hard” distinction referred to above, whereas other authors differentiate Euroscepticism following the specific objects of public criticism, as opposition to the “authorities”, the “regime”, and the “community” of the EU (Serricchio et al., 2013).

## 2.2 Attitudinal versus electoral Euroscepticism

Both soft and hard Euroscepticism can be quantitatively studied from two perspectives: as an attitude or feeling towards European integration, or as a political stance against Europe, manifested through voting for parties that share anti-European agendas. Whereas the former looks at attitudes collected through national or European surveys, the latter looks at the electoral performance of Eurosceptic parties. The first approach is usually preferred because of the availability of information. Due to the European Commission’s Eurobarometer polls, coherent survey-based series on soft- and hard-Eurosceptic attitudes are available. Eurobarometer data series contain, in fact, questions related to both “opposition to membership” (which can be qualified as “hard” Euroscepticism) and “mistrust in the EU” (which can be considered a measure

of soft Euroscepticism). Differently, studying electoral Euroscepticism requires the ex-novo construction of an ad-hoc database, including making potentially controversial decisions concerning which parties should be qualified as Eurosceptic.

Quantitative analyses have been either focused on attitudinal Euroscepticism or limited to electoral behaviour in selected countries, in an attempt to explain individual factors affecting one's decision to cast a vote in favour of a Eurosceptic party. Moreover, only a handful of studies have adopted both a European-wide perspective and a focus on macro determinants. Serricchio et al. (2013) adopt as a measure of attitudinal Euroscepticism the often-used Eurobarometer data on EU membership opposition, transformed into a binary dependent variable, whereas Gomez (2014) builds an index of Euroscepticism that captures a broader definition of Euroscepticism. The main result of Serricchio et al. (2013) is the rejection of the overall relevance of economic factors in explaining membership opposition and the identification of a strong effect of exclusive national identity on Euroscepticism; they consider domestic political attitudes far more important than economic factors in explaining the rise of hard Euroscepticism. Gomez (2014) finds, instead, that when looking to a broader measure of Euroscepticism in the period 2007-2011, economics and unemployment have an effect. One explanation of this divergence is that the degree of rejection of the EU deteriorates over time when the economic situation worsens: In 2011, in the early days of the Eurocrisis, hard Euroscepticism had not yet emerged. A timeline longer than the one adopted in both studies is therefore needed to detect instances of hard Euroscepticism that may threaten European integration.

In addition, electoral data may be more suited to detect instances of politically relevant hard Euroscepticism. It can be argued that an attitude or a feeling acquires political relevance only when citizens are ready to translate it into the ballots. Looking at electoral Euroscepticism helps "clean" our measure of Euroscepticism of those individuals who are ready to report a very hard stance against Europe in the survey but are not ready to act accordingly at the moment of the election. Looking at Electoral Euroscepticism would thus provide more useful information to the extent that it helps quantify the political risks associated with Euroscepticism and not only individuals' attitudes towards "*integration fatigue*". This paper focuses, therefore, on extreme electoral Euroscepticism in the timeframe 2008-2015.

### 2.3 *The crisis and Euroscepticism: Theories and existing evidence*

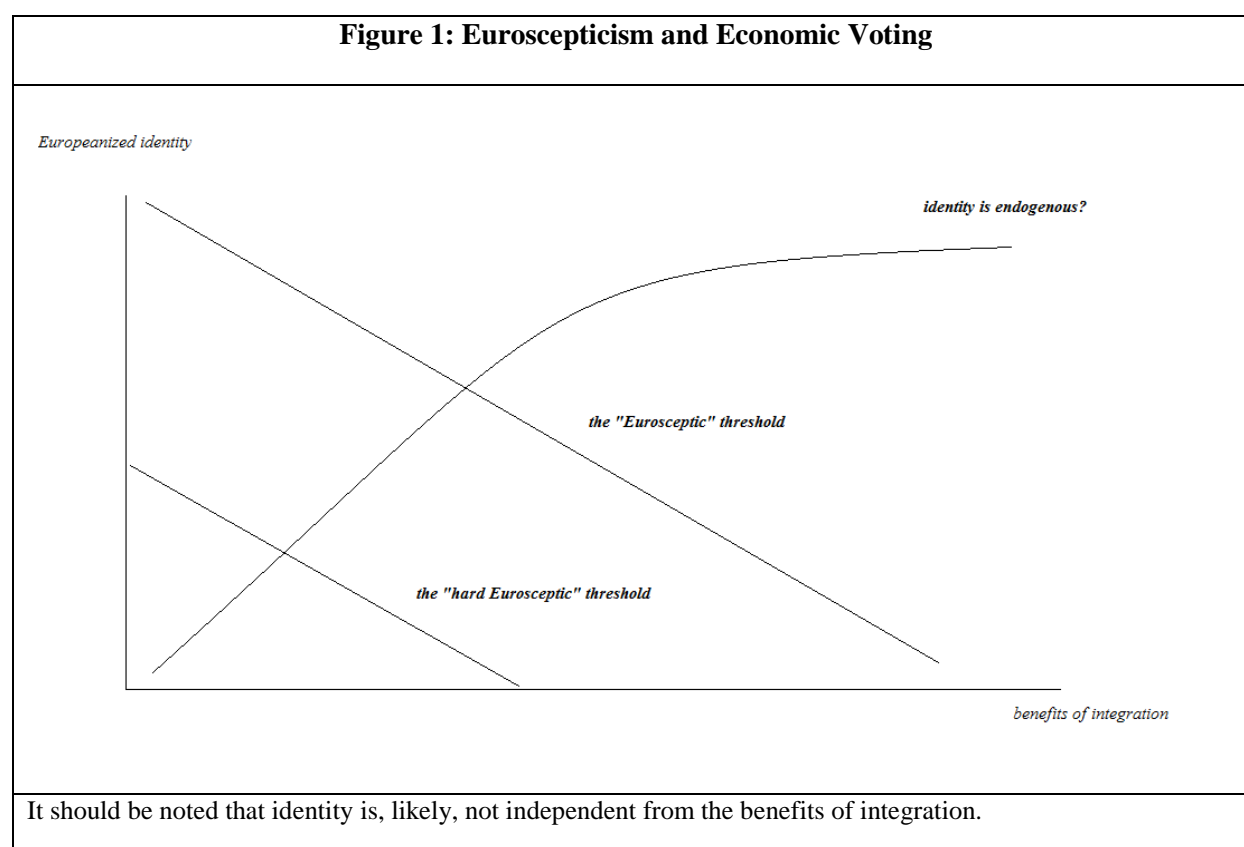
Why would a sustained economic crisis strengthen the consensus for extreme Eurosceptic parties? Several mechanisms could be theorized; we discuss, in particular, economic voting (in its various declinations) and sovereignty losses due to crisis-led integration.

The first reason for Eurosceptic parties to gain in periods of protracted economic crisis could be an “Europeanized” version of economic voting/the failure of output legitimacy of the EU. Economic voting theory predicts that poor economic performance results in an increased consensus for opposition parties. However, the EU is not an input-legitimized polity; therefore, in the absence of classical majority-opposition dynamics, *opposition in the system* becomes *opposition to the system* (Castelli Gattinara and Froio, 2014). Economic voting arguments connect with the idea that the EU is rather “output-legitimised” (Scharpf, 1970; 1999); therefore, if the economic policy implemented thorough the European institutions is perceived as underperforming or even strongly negative, output legitimacy (of the institutions) would disappear (Rohrschneider, 2002; Scharpf, 2009), leading to a surge in parties that oppose the EU rather than those that simply call for a change in policies. Such an effect will be reinforced even when the responsibility of the crisis is attributed to the structural effect of an economic institution (such as the Euro) rather than a policy (such as austerity). Similarly, Euroscepticism can be perceived as a reaction of the “losers” of integration, whose numbers have been perceivably enlarged during the crisis. Empirically, the debate on the magnitude of these effects in the context of the Eurocrisis is open. Whereas early studies (Eichenberg and Dalton, 2007; Serricchio et al, 2013; Gomez, 2014) have tended to downplay the role of economic performance in shaping hard-Eurosceptic attitudes, their datasets end too early (respectively, in 2004 and in 2011) to detect the growth of hard Euroscepticism that may have followed the Eurocrisis beginning in late 2010.

Economic voting also relates to trust in mainstream parties. Eurosceptic parties might try to capitalize on the fall of confidence experienced by traditional mainstream parties in times of economic turndown, as theorized by Anderson and Caltenthaler (1996), Anderson (1998) and Bellucci et al. (2012). Both phenomena (a lack of confidence in mainstream parties and poor economic performance) may boost the

consensus for Eurosceptic parties, particularly to the extent that economic decision making is perceived as super-imposed by European institutions. It must be noted, however, that the relation between trust in the domestic party system and Euroscepticism is at best disputed in the empirical literature. Whereas Anderson (1998) considers that high levels of trust in national institutions and parties positively affect people's attitude towards the EU, Sanchez-Cuenca (2000) finds that when consensus for national institutions and parties is low, the electorate might consider the institutions perceived as "external" as more trustworthy than national ones. Rorhrshenider (2002), however, finds no evidence of a direct effect of quality of domestic institutions on satisfaction for EU democracy, finding instead that the effect is mediated by satisfaction with national democracy.

**Figure 1: Euroscepticism and Economic Voting**



The "economic voting" rationale is pictured in figure 1: as the perceived benefits of integration increase, voters should be increasingly less attracted by voting for Eurosceptic parties, given a certain degree of European identity. Left of the diagonal line, the combination of identity and benefits is not sufficient for voters to support European integration; right of the line, it is. The negative slope is determined by a



compensation effect, as voters with higher European identities are willing to support integration with lower benefits than others. Of course, “Hard-Eurosceptic” voters are likely to gather close to the origins of the axis; soft Eurosceptic voters are somehow closer to the threshold.

Second, Euroscepticism could manifest as a reaction to the loss of sovereignty entailed in the crisis-led strengthening of the new Economic Governance. In fact, the Euro Area is moving towards fiscal and economic integration, having achieved substantial progress during the crisis (Nicoli, 2015). Several policies have been reformed (the Stability and Growth Pact, the European Semester), strengthening the EU’s powers in national policies; new institutions (the Banking Union, the European Stability Mechanism) have been introduced; two new treaties have been signed. Furthermore, the Euro Area path towards fiscal federation is just in its early phases, as anticipated by the 2015 Five Presidents Report. This implies, at best, a reduction in the space of action of national decision-makers, which may be perceived as a loss of national sovereignty and thus lead to a surge in consensus for nationalistic and Eurosceptic parties. Similarly, this shift in competences may provoke a reaction by segments of the population who perceive their national identity to be threatened (Bellucci et al, 2012). In sum, as the Eurocrisis pushes the EU much further beyond the purely pro-market organization it used to be at its inception, the progressive politicization-without-politics (Schmidt, 2015) may entail “*the end of the market Honeymoon*” (De Witte and Hartmann, 2013) and a subsequent rise of parties that oppose the very concept of European integration.

Finally, mediatization of the Eurocrisis may have strengthened the rise of Eurosceptic parties (Kriesi, 2013; De Wilde et al., 2014). The success of a Eurosceptic party in one country could encourage political entrepreneurs to mobilize consensus through similar mechanisms in their own countries (Hooghe and Marks, 2008:19). This may be further strengthened by a “national bias” of still-national media, which could lend more visibility to national politicians with respect to European policy-makers, creating space for the blaming game often played by national actors regarding the EU. In this regard, Ioannou et al. (2015) find evidence for “contagion” mediated (likely) by media: The worsening of the economic situation in a country affects the degree of Euroscepticism in others.

Despite the large amount of theorization on the phenomenon, there is a lack of European-wide discussion on electoral Euroscepticism. Most empirical studies adopt either a country-specific, case study approach with a focus on individual parties or a European-wide approach with a focus on attitudes. In the first group, for example, Startin and Krouwel (2013) discuss France and the Netherlands; Serricchio (2012) and Castelli-Gattinara and Froio (2014) examine the Italian case; Fitzgibbon (2013), the Anglo-Saxon world and Denmark; Grimm (2015), the AFD's rise in Germany; Verney (2015), the Greek case; Reungoat, (2015), the French case. In the second group, the focus has been—due to the availability of the Eurobarometer data series—on attitudinal Euroscepticism in the period before the European crisis, including Eichenberg and Dalton (2007), Serricchio et al. (2013), and more recently Bargaoanu, Radu and Negrea-Basuioc (2014), Dobrescu and Durac (2014), Gomez (2014) and Ioannou et al. (2015). A particular case is constituted by Taggart and Szczerbiak (2013), who adopt a European-wide, party-focused approach. However, their focus is more on soft Euroscepticism as they investigate the consequences of Eurosceptic parties' participation in governments; therefore, their contribution to identifying the causes behind the European trend is limited. By focusing on electoral hard Euroscepticism in the timeframe 2008-2015, this paper aims to fill a gap in the existing literature by exploring the role of economic performance in strengthening Eurosceptic parties. We explore, in particular, whether (1) unemployment and (2) governance and the economic cycle affect the votes for Eurosceptic parties. Whether economics affects Euroscepticism is a controversial topic in recent literature: Serricchio et al. (2013) give a negative response to (1) and (2), whereas Gomez (2014) and Ioannou et al (2015) seem to believe that economics has indeed affected at least soft Euroscepticism. Because the crisis worsened in several countries after 2011 and a “spillover effect” is identified by Ioannou et al. (2015), our first hypothesis (H1) is that *“the share of votes for Eurosceptic Parties will increase as the economic performance of the country worsens, provided that economic sovereignty was transferred and given a set of controls”*. We also expect (H2) that governance settings implying an increase in European interference with domestic economic policy-making also positively affect consensus for anti-European parties.

### 3. Quantifying extreme electoral Euroscepticism

#### 3.1 Data collection

The previous sections have defined the scope of this study by discussing the motivations behind the choice of electoral, hard Euroscepticism. Thus, the dependent variable for extreme electoral Euroscepticism is defined as follows:

*“the cumulative share of votes obtained by parties sharing a hard-Eurosceptic agenda in national and European elections”.*

To qualify for inclusion in the extreme Euroscepticism dependent variable, a party must have in its electoral programme a claim in favour of the reduction of the level of integration by means of unilateral exit from the Euro Area or the European Union and by means of comprehensive treaty change.<sup>62</sup> As explained in the previous section, identifying which parties share extreme-Eurosceptic agendas may be problematic. For a total of 108 elections in Europe since 2009, the following multi-step methodology is adopted.<sup>63</sup> First, we exclude from the analysis pro-Europe, mainstream parties affiliated with PES, EPP, the European Green Party, and the Alde Party. Second, we qualify as “extreme Eurosceptic” any party associated with the EFD and ENF groups in the European Parliament in the 2009-2014 legislature.

The remaining parties are analysed following a two-steps-plus approach. This concerns, in particular, parties affiliated the ECR group because a minority of the ECR-associated parties have strong anti-European views; the same applies for a subset of strong-Eurosceptic parties on the left side of the spectrum. First, we select all remaining parties that have a score of at least 0.5 on the European Manifesto Project database. Second, of all selected parties, we drop parties ranking 3 or above on the Chapel Hill Survey.<sup>64</sup>

For the remaining non-attached and non-elected parties (above 1.5% of the votes), their electoral platforms are analysed to detect signs of extreme Euroscepticism, as described above. The operation is repeated for

---

<sup>62</sup> Treaties considered do not include the two inter-governmental treaties signed since 2011 (ESM and TSCG) because they do not represent a part of the aquis.

<sup>63</sup> Annex 1 provides a complete list of concerned parties.

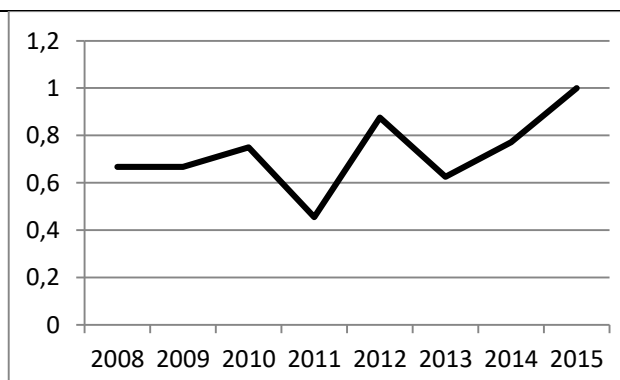
<sup>64</sup> In some cases, extra attention is paid to the particular political context of the country; this is the case for Greece, the UK and Spain. In the latter case, it has been chosen to qualify Podemos as a hard-Eurosceptic party, although it formally does not qualify as Eurosceptic. The decision is based on the claim in the 2014 Electoral manifesto for a Spain opt-out from the Lisbon Treaty and on existing literature (for instance Bertoni and Koenig, 2014). Furthermore, it was suggested in an expert interview that Podemos constitutes the only instance of Euroscepticism in Spain, thus catalyzing all Eurosceptic votes despite its non-extreme stance on European issues.

each election since 2008 for a total of 108 observations.<sup>65</sup> The share of the total electoral episodes in which Eurosceptic parties have obtained more than 5% of the votes is reported in figure 1 below, showing a clear upward trend.

### 3.2 Electoral Euroscepticism in figures

Before proceeding with econometric analysis, we briefly show data trends. Figure 1 presents the share of elections in which Eurosceptic parties have achieved more than 5% of the votes, with a clear “double-pick” in suggestive correspondence with the economy’s “double-dip”. More in detail, several countries have experienced a rise of Euroscepticism during the Crisis: France, Italy, Greece, Sweden, Cyprus, Poland and Spain (Annex 2). Other countries—Austria, the United Kingdom, Denmark and Austria—have shown a V-shaped effect, with a downturn in consensus for Eurosceptic parties that rapidly peaked again during the 2014 European elections (the latest observation for most countries). The only countries with a clear downward trend appear to be Belgium, the Netherlands and the Czech Republic, whereas the remaining countries show an unclear trend.

**Figure 2- share of elections with Eurosceptic parties achieving more than 5% of the votes.**



<sup>65</sup> After testing, no statistically significant autocorrelation is found in the DV.

### 3.3. *The model*

The set of independent variables includes variables aiming to assess the effect of mistrust in domestic politics on Euroscepticism, economic indicators, policy indicators and institutional indicators (table 2). The (unbalanced) panel is composed of 108 observations in 27 countries (the EU minus Croatia), from a minimum of 3 to a maximum of 6 observations per country; the data for independent variables are collected by multiple established sources, as indicated in table 1.

When looking at panel data, we have three main alternative approaches: fixed effects, random effects and pooled OLS. A fourth possibility is the Hausman-Taylor endogenous variables regression, which combines fixed effects and random effects. In principle, we would like to control for time-invariant known factors that may play an important role in determining the rise of Eurosceptic parties. Furthermore, we believe that observed differences across entities may have an effect on voting for Eurosceptic parties.

In general, interest in time-invariant variables should make random effects more suitable, if it is consistent with the hypothesis that the panel-specific errors are not correlated with the regressors. Perfect independence, of course, can rarely be achieved, so a random-effects model will always suffer some bias. However, including in the model specification as many as time-invariant variables as possible should decrease the magnitude of the bias. The random-effects model is tested against the fixed-effects alternative through a Hausman specification test. When consistent with Hausman test results, the random effects estimates are reported.<sup>66</sup> In this regard, we opt for a random-effects model that specifies various country-specific factors on the right end of the equation to minimize the risk of omitted variable bias.

---

<sup>66</sup> To address potential heteroskedasticity, robust standard errors should be adopted. However, the standard version of the Hausman test requires a homoscedasticity assumption. To address potential heteroskedasticity, we decide to proceed with a double testing approach, using two alternatives: the standard Hausman test and the auxiliary regression procedure (Mundlack, 1978; Woolridge, 2010). The normal Hausman test is passed for all specifications; the *xtoverid* cluster-robust version is passed for models A4, A3, A1.

Of particular interest are the three indicators of mistrust: Once considered together, the first captures the effect of mistrust in national party systems, whereas the second captures the effect of changes that occurred just before the election, and the third identifies the overall loss of credibility during the crisis.

I expect their coefficients to be positive, thus indicating that an increase in party mistrust increases consensus for Eurosceptic parties. Economic indicators such as GDP growth during and before the elections, as well as the cumulative effects since the crisis, may also provide interesting information. We expect them to be negative, indicating that short- and long-term improvements in economic performance have a negative effect on Euroscepticism. The same applies to the several indicators of unemployment, whose coefficients we expect to be positive: As the unemployment level increases, Eurosceptic parties benefit more.

I also include the size of financial assistance provided or received (in absolute values), which may shed light on the political costs of integration in both debtor and creditor countries. *Smallcountry* is taken into account as a control variable because electoral dynamics and interactions in small communities may play an important role in shaping voting behaviour; similarly, new member states are accounted for through the control *easternEurope*. Controls also include compulsory voting (which may increase the participation of non-mobilized electors, which tend to align with the mainstream) and several IVs that try to catch the heterogeneity of each election (turnout, type of election—presidential or second order—early election).

Table 1- List of Covariates
-----------------------------

Var name	Description	Source	Unit of Measure
AntiEUScore	Dependent variable. share of votes of hard-Eurosceptic parties	National Electoral Offices, European Parliament	% of valid votes
avg_PartyMistrust	Degree of mistrust in the Party System in the given quarter	Eurobarometer	% of the respondents
D_base_PartyMistrust	Change in the degree of mistrust in the Party System in respect to the base period (2005- 2008)	Own calculations based on Eurobarometer	% points of change
D_PartyMistrust	Degree of mistrust in the Party System in the given quarter, change on the previous quarter	Eurobarometer	% points changed
Compulsoryvoting	The country has in place a compulsory voting system	Gratschew M. (201	Binary variable
Netassistance_abs	The country has given or received financial assistance.	EU Commission	Bn Euros, absolute value
SixPack	The election takes place after the introduction of the new economic governance	EU Commission	Binary variable
Eamember	The country is a Euro Area member	EU Commission	Binary variable
Presidentialcountry	The Country has in place a presidential or semi-presidential system		Binary variable
PresidentialElection	The election is a presidential or semipresidential first-turn election		Binary variable
EasternEurope	Post-2004 countries		Binary variable
Secondorder	The election is an European election	European Parliament	Binary variable
smallcountry	The country has less than 2 million citizens	Eurostat	Binary variable
earlyelection	The election occurred before the formal expiration of the mandate	National Electoral offices	Binary variable
avg_growth	Average growth rate in the two quarters of the election	Eurostat	% of GDP
D_baseGDP	Change in absolute GDP figures from the base year (2008)	Eurostat	% of 2008 GDP
avg_Unemployment	Average unemployment rate in the two quarters of the election	Eurostat	% of the active population
D_Unemployment	Change in unemployment rate in respect to the quarter before the election	Eurostat	% of the active population
D_baseUnemployment	Change in unemployment rate from the base period (average 2005-2008)	Eurostat	% points changed
H_Uduration	Number of sequential quarters with unemployment rate above the base period (average 2005-2008)	Own calculations based on Eurostat	Number of quarters
Turnout	Electoral participation in the election	National Electoral Offices; European Parliament	% of the total electorate

In sum, the model expects that a substantial share of voting for Eurosceptic parties is explained by:

(1) political trust factors ( $avg\_PartyMistrust + D\_PartyMistrust + D\_basePartyMistrust$ )

(2) economic factors ( $avg\_GDP + D\_baseGDP + avg\_Unemployment + hU\_duration$ )

(3) governance factors ( $netassistance\_abs + EAmember + SixPack$ ),

a set of controls (4) including observation-, country- and election-specific factors ( $compulsoryvoting + smallcountry + eastEurope + presidentialelection + turnout + earlyelection$ ).

Equation 1 recalls the random-effects model including all variables (specification A5):

(1) *AntiEUScore*

$$\begin{aligned} = & \alpha + \beta_1 avgPartyMistrust_{it} + \beta_2 \Delta PartyMistrust_{it} + \beta_3 avgGDP_{it} \\ & + \beta_4 \Delta baseGDP_{it} + \beta_5 avgUnemployment_{it} + \beta_6 hU.duration_{it} \\ & + \beta_7 netassistance_{abs_{it}} + \beta_8 EAmember_{it} + \beta_9 compulsoryvoting_{it} \\ & + \beta_{10} smallcountry_i + \beta_{11} presidentialelection_{it} \end{aligned}$$

$+ \beta_{12} turnout_{it} + \beta_{13} earlyelection_{it} + \beta_{14} SixPack + \beta_{15} eastEurope_i + u_i + \varepsilon_{it}$  whereby  $u_{it}$  and  $\varepsilon_{it}$  constitute, respectively, the across-groups and within-groups error terms,  $i$  is the 27 member states, and  $t$  is the time of the observation. Six different specifications of the model are tested, comparing different sets of variables.<sup>67</sup>

#### 4. Results

Five alternative random-effects specifications are run. The first model (A1) looks specifically into short-term political trust effects by excluding the series of independent variables referring to economic factors and long-term trust changes. The second model (A2) includes GDP effects; the third model (A3) includes trust and unemployment effects but excludes GDP effects; the fourth model (A4) includes both GDP and unemployment effects but excludes trust effects; (A5) includes all variables. Table 2 reports the coefficients and the robust standard errors (in parentheses) of the independent variables.

<sup>67</sup> Note that *compulsoryvoting*, *EastEurope*, and *smallcountry* are time-invariant variables.



#### 4.1 Political trust

As noted in the surveyed literature, there is disagreement regarding the effect of trust in the domestic system on Euroscepticism: Anderson (1998) considers that higher trust in the national political system may increase trust in the EU (and the other way around), whereas Sanchez-Cuenca (2000) believes that when confidence in the domestic political system is low, citizens look abroad to find examples of good government and best practices. However, the results shown in table 2 fail to shed light on the relation between Euroscepticism and trust in domestic political parties.

When included in the specification, party mistrust is not statistically significant and has a very small associated coefficient. In particular, we find almost no support for the effect hypothesized by Sanchez-Cuenca (2000), according to which Europe, providing an external constraint to national politicians, is perceived more positively as voters' confidence in domestic parties decreases. For this suggestion be true, the coefficient of mistrust (*avg\_PartyMistrust*) either has to be negative or has to turn negative once long-term rises detected by the *D\_basePartyMistrust* indicator are controlled for. If this were the case, it would have suggested that long-term, stable mistrust in domestic parties could lead people to accord more consensus to parties that support European Integration because Europe is perceived as a positive "external" constraint on mistrusted domestic politics. Specifications A1 and A5, which account for this possibility, fail to provide conclusive evidence: Whereas the coefficient of *avg\_PartyMistrust* behaves as expected, being negative when *D\_BasePartyMistrust* is included, both variables fail to be statistically significant, thus leaving the question largely unanswered.

#### 4.2 Economy and governance

In accordance with our first hypothesis, we expect to see Euroscepticism increase with both worsening economic performance and rising unemployment. Concerning overall economic performance, in each of the specifications of the random-effects model, the effects of the average GDP growth rate in the quarters around the election seem to meet our expectations. Differently from Serricchio et al. (2013), it holds a negative coefficient, as expected (i.e., as pre-election downturn becomes stronger, the share of votes for

Eurosceptic parties becomes larger) and is statistically significant, albeit at 5% and 10% confidence levels. The sign of the coefficient for the long-term economic loss captured by *D\_base\_GDP* is, as expected, negative, but it fails to be statistically significant in all specifications.

The model also includes two unemployment measures: *avg\_unemployment*, which captures the average level of unemployment in the two quarters before the election, and *hU\_duration*, which captures the number of consequent quarters with an unemployment rate above the pre-crisis average at the moment of the election.

Table 2: random-effects specifications

	A1	A2	A3	A4	A5
<i>avg_PartyMistrust</i>	-0.108 (0.93)	-0.083 (0.67)	-0.072 (0.54)		-0.055 (0.40)
<i>D_base_PartyMistrust</i>	0.091 (0.93)	0.070 (0.68)	0.093 (0.90)		0.069 (0.64)
<i>avg_growth</i>		-0.355 (1.40)		-0.555 (2.26)**	-0.516 (2.06)**
<i>D_base_GDP</i>		0.023 (0.39)		-0.037 (0.58)	-0.039 (0.59)
<i>avg_Unemployment</i>			-0.347 (1.97)**	-0.398 (2.37)**	-0.406 (2.04)**
<i>hU_duration</i>			0.136 (1.34)	0.187 (1.72)*	0.182 (1.69)*
<i>SixPack</i>	2.443 (2.31)**	2.727 (1.80)*	1.157 (0.93)	2.005 (1.33)	2.016 (1.34)
<i>Eamember</i>	-1.309 (0.62)	-1.515 (0.69)	-2.264 (1.15)	-2.103 (1.03)	-1.955 (0.92)
<i>smallcountry</i>	-6.493 (1.86)*	-6.452 (1.78)*	-5.840 (1.69)*	-5.691 (1.82)*	-6.029 (1.71)*
<i>secondorder</i>	1.501 (1.23)	1.312 (1.06)	1.187 (1.00)	0.876 (0.77)	0.830 (0.71)
<i>turnout</i>	0.013 (0.25)	0.021 (0.39)	0.005 (0.10)	0.026 (0.57)	0.025 (0.51)
<i>netassistance_absB</i>	0.003 (2.53)**	0.003 (2.09)**	0.004 (2.46)**	0.004 (2.28)**	0.004 (2.30)**
<i>easterneurope</i>	-1.517 (0.51)	-1.776 (0.59)	-1.884 (0.69)	-2.664 (0.92)	-1.841 (0.66)
<i>presidentialelection</i>	-1.584 (1.58)	-1.777 (1.69)*	-1.690 (1.38)	-2.267 (2.26)**	-2.178 (1.99)**
<i>compulsoryvoting</i>	-6.133 (2.40)**	-6.278 (2.47)**	-6.000 (2.23)**	-6.172 (2.45)**	-6.370 (2.43)**
<i>_cons</i>	18.266 (1.58)	16.070 (1.33)	19.416 (1.60)	12.950 (2.48)**	16.852 (1.37)
<i>N</i>	108	108	108	108	108
<i>R<sup>2</sup></i>	0.276	0.282	0.331	0.375	0.366
<i>Hausman</i>	Passed	Passed	Passed	Passed	Passed
<i>Hausman-Robust</i>	Passed	failed	Passed	Passed	failed

\*  $p < 0.1$ ; \*\*  $p < 0.05$ ; \*\*\*  $p < 0.01$

The results reported in table 2 are challenging: The sign of the average unemployment level is consistently statistically significant and negative, whereas the duration of high-level unemployment is consistently significant and positive.<sup>68</sup> One possible explanation for this effect is the geographical distribution of unemployment and Euroscepticism. Although several northern countries have enjoyed low levels of unemployment, they have nonetheless developed strong Eurosceptic parties in opposition to bail-out programmes for southern states (e.g., the case of Finland's True Finns; Raunio, 2012). In contrast, Southern European countries with very high levels of unemployment have seen the electoral emergence of Eurosceptic forces only some years after the beginning of the crisis (Italy after 2013; Spain in 2014). The results seem to suggest that voters attribute to the EU the responsibility in failing to address the crisis rather than blaming it for the crisis itself.

The apparent divergent effect of unemployment may also be related to our second hypothesis, the domestic effect of economic governance. When looking at net contributions to the bailout programmes (expressed in absolute values so that both a very high contribution and very high financial support have a positive sign), the model shows a very small but highly significant effect on Euroscepticism. The same applies to the effect of the introduction of the European Semester, although the use of a dummy variable implies some caution in interpreting the result.<sup>69</sup> In fact, the correlation between the unemployment rate and non-zero net contributions to the bailout scheme is positive (0.63): Countries with lower unemployment rates have also paid more into the scheme, hence the double effect on *avg\_Unemployment* and *netassistance\_absB*.<sup>70</sup>

#### 4.3 The controls

---

<sup>68</sup> The two variables are only loosely correlated (0.37); moreover, when run in separate regressions, neither the statistical significance nor the size and sign of the coefficient varies noticeably, suggesting that the divergent effect is not due to multicollinearity.

<sup>69</sup> A different measure of governance (derived from a normalized version (2008=1)) of the integration index developed by Dorucci et al. (2015)) is also tested: This alternative measure, however, provides no added value to the analysis and therefore is not included in this study.

<sup>70</sup> Second-order elections are controlled through a dummy variable, but it cannot account for interactions between other IVs and the type of election. To address this, interaction terms are added for the four main IVs: unemployment duration, average unemployment, average growth, and average party mistrust. A joint test is performed to evaluate their significance, which is rejected. The marginal effects of the four main IVs on the type of election, computed as first derivatives (Kam and Franzese, 2007), equally fail to be statistically significant. Therefore, no significant interaction effect is found.

In all models, Euro Area Membership fails to pass the significance test at the 10% confidence interval, as do second-order elections and eastern Europe. Among all controls, presidential elections and the existence of compulsory voting legislation turn out to be statistically significant in all models at the 5% confidence level (10% in A1 and A2). Voters who otherwise would not care about participating in the election spend little time developing extreme political positions (which are somewhat required to vote for a extreme Eurosceptic party), thus concentrating towards moderate, status-quo mainstream parties. Finally, the effect related to country size is statistically significant at the 10% level in specifications 1, 2 and 4.<sup>71</sup>

## 5. Conclusions

Overall, the results show evidence of an effect of the crisis on the rise of extreme Eurosceptic parties, particularly through the channel of negative growth, the duration of historically high levels of unemployment, and governance arrangements, supporting earlier evidence from Gomez (2014 and Ioannou et al (2015). In contrast, membership of the monetary union, as such, fails to appear to be a directly relevant factor even when economic variables are accounted for; the same applies to the lack of trust in the domestic political system. These results suggest that the legitimacy of the EU still depends on its performance. This finding constitutes a warning for policy-makers: Negative performance may further erode the EU's output legitimacy, weakening support for integration and strengthening Eurosceptic parties even more.

Further research may benefit from strengthening the quality of policy variables included, particularly in relation to the introduction of the incremental stages of the new economic governance since 2011. Furthermore, more solid results would require a longer dataset, which might be obtained both by including new elections as they occur and by stretching further back in the past the range of electoral episodes accounted for. Moreover, some caution is required in generalizing these results. On the one hand, the paper

---

<sup>71</sup> *Robustness checks.* The existence of random effects, suggested by the high p-value of the Hausman tests performed, brings about efficient estimates of the coefficients and of the significance of several variables. A series of robustness checks is performed on specification A4, which shows more statistically significant variables, a higher  $r^2$  and a larger margin in the robust Hausman test than other alternatives. Specification 4 is then tested in a Hausman-Taylor endogenous variables regression (H-T), fixed-effects (FT) and two pooled OLS (robust standard errors for heteroscedasticity and cluster-robust errors for within-panel time dependency) to see whether important differences exist in the estimates. The results are reported in annex 2. The main difference is between FE and the other models. The only relevant difference between the H\_T model and the RE model is that in the latter, *avg\_growth* loses statistical relevance. Unemployment measures tend to maintain sign and significance across models.

adopts a narrow definition of hard Euroscepticism, restricting the analysis to the most vehement anti-European parties. A wider party selection may change the outcome with the inclusion of more mainstream parties in the panel. On the other hand, this research setting is unable to address the dynamic nature of Euroscepticism. First, it does not account for the risk of contagion across a country's political spectrum: The success of one hard-nosed Eurosceptic party may push mainstream parties to weaken their pro-European stance but may not push them completely into full-fledged Euroscepticism. Second, it is still possible that extreme Eurosceptic parties, if successful in their bid to win over a country's government, may moderate their stance once in office. Nevertheless, the paper suggests that in times of crisis, hard-Eurosceptic parties tend to benefit from poor economic performance, possibly as a manifestation of the output-legitimized nature of the EU. Failure to sustain a stable recovery may increase resentment towards the EU, undermining the efforts for further progress in integration.



Annex 1- electoral scores of hard-Eurosceptic parties, % of votes

<i>country-election</i>	<i>antiEUscore</i>		<i>country-election</i>	<i>antiEUscore</i>	
FranceEP2009	12.8	FN, MPF, DLR	CyprusEP2014	2.7	ELAM
FranceP2012	19.7	FN, DLR	LuxembourgEP2009	<1	
FranceLeg2012	13.6	FN	LuxembourgGE2009	<1	
FranceEP2014	28.6	FN, DLR	LuxembourgGE2013	<1	
GermanyEP2009	1.3	REP	LuxembourgEP2014	<1	
GermanyF2009	1.8	NDP	MaltaEP2009	<1	
GermanyF2013	6	AFD, NDP	MaltaPE2013	<1	
GermanyEP2014	8.0	AFD, NDP	MaltaEP2014	<1	
ItalyGE2008	10.7	LN, LD-FT	BelgiumEP2009	9.85	VB
ItalyEP2009	13.2	LN, A, FT	BelgiumFE2010	10	VB
ItalyGE2013	29.6	LN, FdI, LD, M5S	BelgiumEP2014	4.1	VB
ItalyEP2014	31	LN, FdI, M5S	BelgiumFE2014	5.84	VB
GreeceEP2009	15.5	LAOS, KKE	polandEP2009	2	PR
GreeceLE2009	13.3	LAOS, KKE, XA	polandPE2011	1.4	KNP, PR
GreeceLE2012May	29	LAOS, KKE, XA, ANEL	PolandEP2014	12.44	KNP, SPZZ
GreeceLE2012June	20.5	LAOS, KKE, XA, ANEL	UKEP2009	26	UKIP, BNP, ED, N2EU
GreeceEP2014	21.4	LAOS, KKE, XA, ANEL	UKGE2010	5.8	UKIP, BNP, ED, DUP
GreeceLE2015	17.5	LAOS, KKE, XA, ANEL	UKEP2014	30.8	UKIP, BNP, ED, DUP, IFE
PortugalEP2009	10.7	BE	DenmarkEP2009	21.8	O, N
PortugalLE2009	10	BE, ND	DenmarkGE2011	12.3	O
PortugalPR2011	4.5	ND	DenmarkEP2014	34.6	O, N
PortugalLE2011	5.5	BE, ND	SwedenEP2009	6.82	JL, SD
PortugalEP2014	5.1	BE, ND	SwedenGE2010	5.7	SD
the NetherlandsEP2009	23.80	PVV, CU	SwedenEP2014	9.7	SD
the NetherlandsGE2010	18.6	PVV, CU, PVD	Sweden GE2014	12.86	SD
the NetherlandsGE2012	15.1	PVV, CU, PVD	RomaniaEP2009	8.65	PRM
the NetherlandsEP2014	20.1	PVV, CU	RomaniaPR2009	7.5	PRM, PNGCD
AustriaLE2008	26.8	FPO, BZO	RomaniaPE2012	16.12	PRM, PP
AustriaEP2009	17.3	FPO, BZO	RomaniaEP2014	6.37	PRM, PP
AustriaPE2013	20.3	FPO, BZO	RomaniaPR2014	7.72	PRM, PP
AustriaEP2014	22.5	FPO, EUSTOP	BulgariaEP2009	14.21	PPA, BMPO
EstoniaEP2009	2.2	RL	BulgariaPE2009	9.5	PPA
EstoniaPE2011	2.6	RL, EIP	BulgariaPE2013	12.9	PPA, NFSB
EstoniaEP2014	5.3	EKRE, EIP	BulgariaEP2014	6	PPA, NFSB
EstoniaPE2015	8.3	EKRE, EIP	BulgariaPE2014	11.8	PPA, PF
IrelandEP2009	8.1	L, SP	LatviaEP2009	14.55	TB, L, VL
IrelandGE2011	2.6	DDI, PBP, SP	LatviaPE2010	7.8	NA (TB, VL)
IrelandEP2014	4.8	DDI, PBP, SP	LatviaPE2011	13.88	NA (TB, VL)
SloveniaEP2009	2.85	SNS	LatviaEP2014	14.4	NA (TB, VL)
SloveniaPE2011	1.8	SNS	LatviaPE2014	16.6	NA (TB, VL)
SloveniaEP2014	4.4	SNS	Czech republicEP2009	5.52	CS, SVOBODNI
SloveniaPE2014	2.2	SNS	CzrepublicLE2010	4.41	CS, SVOBODNI
SlovakiaEP2009	5.6	SNS	CzrepublicLE2013	10.06	UNSVIT, SVOBODNI, CS
SlovakiaPE2010	5.1	SNS	CzrepublicEP2014	8.36	UNSVIT, SVOBODNI
SlovakiaPE2012	4.5	SNS	czrepublicSEN2014	2.71	UNSVIT, SVOBODNI
SlovakiaEP2014	5.3	SNS, L'SNS	LithuaniaEP2009	20.1	TT
FinlandEP2009	9.7	PS	LithuaniaPE2012	13.1	TT
FinlandGE2011	19.1	PS	LithuaniaEP2014	14.27	TT
FinlandEP2014	12.9	PS	HungaryEP2009	14.77	JOBBIK
SpainGE2008	<1		HungaryPE2010	16.7	JOBBIK
SpainEP2009	<1		HungaryPE2014	20.5	JOBBIK
SpainGE2011	<1		HungaryEP2014	14.7	JOBBIK
SpainEP2014	7.97	Podemos			
CyprusEP2009	<1				
CyprusPE2011	<1				
CyprusPR2013	<1				

## Annex 2

## Annex 2- comparison of models

	Random Effects	Fixed Effects	Hausman-Taylor	Pooled OLS (robust)	Pooled OLS (cluster-robust)
[compulsoryvoting]	-6.172 (2.45)**		-6.313 (1.24)	-7.226 (2.89)***	-7.226 (2.19)**
avg_growth	-0.555 (2.26)**	-0.475 (2.20)**	-0.575 (1.33)	-1.020 (1.97)*	-1.020 (2.32)**
D_base_GDP	-0.037 (0.58)	0.003 (0.04)	-0.024 (0.26)	-0.175 (1.90)*	-0.175 (1.60)
(avg_Unemployment)	-0.398 (2.37)**	-0.241 (1.28)	-0.315 (1.38)	-0.574 (2.88)***	-0.574 (1.99)*
(hU_duration)	0.187 (1.72)*	0.117 (1.01)	0.175 (1.71)*	0.290 (2.84)***	0.290 (2.16)**
SixPack	2.005 (1.33)	1.785 (1.11)	1.994 (1.15)	3.376 (1.73)*	3.376 (1.96)*
Eamember	-2.103 (1.03)	0.603 (0.26)	-2.001 (0.84)	-2.833 (1.35)	-2.833 (0.93)
[Smallcountry]	-5.691 (1.82)*		-5.547 (1.66)*	-5.021 (2.55)**	-5.021 (1.50)
secondorder	0.876 (0.77)	1.107 (0.91)	1.086 (0.66)	0.714 (0.40)	0.714 (0.45)
tumout	0.026 (0.57)	0.020 (0.43)	0.033 (0.55)	0.078 (1.25)	0.078 (1.17)
(netassistance_absB)	0.004 (2.28)**	0.004 (2.57)**	0.003 (2.26)**	0.004 (1.70)*	0.004 (1.48)
[Easterneurope]	-2.664 (0.92)		-2.432 (0.78)	-2.286 (0.97)	-2.286 (0.73)
presidential election	-2.267 (2.26)**	-1.827 (2.01)*	-2.320 (0.96)	-4.965 (2.41)**	-4.965 (2.17)**
_cons	12.950 (2.48)**	8.110 (1.76)*	11.605 (2.04)**	10.515 (1.87)*	10.515 (1.71)*
N	108	108	108	108	108
R <sup>2</sup>	0.37	0.26		0.41	0.41

\*  $p < 0.1$ ; \*\*  $p < 0.05$ ; \*\*\*  $p < 0.01$ 

Time invariants are in square brackets. Endogenous variables are in parenthesis



# Conclusions

## 1. Introduction

Introducing the conclusion of a project worth years of research is, by itself, a daunting undertaking, although the very drafting of a satisfactory final chapter is, by itself, not easy. In part, this is due –as I wrote in the opening pages of this volume— to the fact that this dissertation is, more than a self-contained exercise, a path-opening work; I expect Crisis theory, Functionalism and Euroscepticism –let alone the Eurocrisis and the reform of the Economic Governance – to walk along my side for many years to come. On the other hand, concluding a three-year research project is complicated by the astonishing simple fact that *time flows*: the world outside, the author, his understanding of the underlying problem and his research design have come a long way since the initial submission in April 2013.<sup>72</sup> To some extent, this is reflected in the incremental nature of the different papers/chapters that compose the thesis; nonetheless, when summarizing the overall results, one should avoid, whenever possible, repetitions from the conclusions of each chapter and the introductions to the following one.

Finally, differently from the several papers/chapters of this dissertation, these conclusions hardly have a

---

<sup>72</sup> Looking back, it is quite impressive how the world used to be back then, just about 40 months ago. There was no migration crisis and no terrorism in Europe; the EU had just won the 2013 Nobel Prize for Peace. Ukraine was still owning Crimea, and Russia was not yet openly in the Rogue States Club; oil was traded above hundred dollars a barrel; Matteo Renzi had just been defeated in the Centre-Left primary elections, and many international observers were relieved that Eurosceptic parties, in Germany, couldn't pass the 5% threshold in the Bundestag election. The United Kingdom was still part of the European Union and Angela Merkel (and her newly-minted, parodic Twitter Account, @Queen\_Europe) had the continent at their whim (not that the latter two have changed just yet, although they have both started looking shaky too).

stand-alone existence. Therefore, one should resist to the temptation to delve into excessive self-analysis and reassessment of its own evolution. This said, it is important to notice that these conclusions do not constitute a stand-alone chapter. Each paper discusses, independently, its own conclusion; the goal of this final part, rather than developing additional thinking, is to present, in an organized and coherent form, the conclusive remarks of each standalone paper. To do so, these conclusions are organized in four parts. First, after having briefly restated the initial research questions, section 2 recalls the *empirical results* of the different papers composing this thesis in light of their contribution in answering the original questions. Then, section 3 discusses the *theoretical findings* developed throughout the dissertation; section 4 analyses the *policy implications* of the findings; and finally, section 5 discusses some final remarks and pathways for future development.

## 2. Empirical results

In the early pages of this dissertation, I stated a theoretically-driven, two tier research problem: first, determining whether the Eurocrisis could be considered as a functional crisis, thus corroborating the validity of Schmitter's Neofunctionalism as a viable theory to understand European integration. Second, the thesis aimed to assess, *once we apply the theory*, whether the Eurocrisis can be considered as a sufficiently strong and generalized crisis to trigger a switch from functional "priming cycles", to politicized, Postfunctional "transforming cycles". This research question has implications far wider than the settlement of a theoretical debate; if, generally, Neofunctionalism is correct, and if the hypothesis concerning the inception of the transformation cycle is correct, it would imply that the Union has reached a point of no-return, where it either moves towards full federalization, or it risks a permanent break-up.

More specifically, a set of general, testable hypotheses has been laid down in the conclusive pages of the first chapter. Testing whether the Eurocrisis is a full-fledged functional crisis requires verifying two conditions: (a1) the crisis *endogeneity*, and (a2) *the functional nature* of its resolution. Likewise, assessing whether the Eurocrisis triggered a transformation cycle requires assessing two fundamental conditions: (b1)

whether it has triggered preferences towards integration of (at least some) key state powers, and whether (b2) it has produced widespread politicization of the political process.

One should note that if (b1) is verified, (b2) is likely to follow on its own, either because (i) the “core state powers” have been integrated along with an appropriate political system, switching the domestic political process upwards; or because (ii) in the absence of an appropriate crisis resolution mechanism, lacking output legitimacy would trigger widespread opposition; or, finally, because (iii) even if appropriate mechanisms are set in place, widespread opposition rises anyway as a consequence of either lacking democratic controlling institutions, or lacking common identity.

### *2.1 Is the Eurocrisis a functional crisis, thereby confirming both hypotheses a1 and a2?*

In short, the Eurocrisis approaches the ideal-type of a functional crisis, although with a specific, domestic component. Chapter 3 demonstrated that, in line with the “consensus view” on the Eurocrisis (Baldwin et al., 2015), the crisis had a two-tier endogenous source. The first endogenous source depends on the missing capacity, at European level, to address the crisis properly; the second endogenous source is the divergent economic performance at domestic level across Eurozone countries in the pre-crisis period, which –albeit the making of national decision-makers— is twin-linked with the crisis. First, because the Eurozone lacked a coordination mechanism to prevent such a divergence; and second, because the threat posed to economic stability by divergence is amplified by the presence of an institutionally-incomplete monetary union.

In terms of crisis resolution (hypothesis a2) the answer is less nuanced. In principle, the resolution of the crisis may take the form of a completely domestic economic adjustment process (thereby without needing competences allocation), although some frictions at Eurozone level may remain (for instance, in terms of labour mobility). However, in practice, a purely domestic solution has always been unlikely, and a substantial share of integration has indeed happened already. More than *whether* the crisis had integrative (or dis-integrative) solutions, it is interesting to understand which type of integration has occurred. Chapter 4 has shown that, while both “spill-arounds” and “spill-overs” have happened during the crisis, the most resolving measures (OMT, Banking Union, EFSI) were clearly of spillover nature; they also produced early

politicization through increased *autonomy* of the institutions in politically-sensitive areas like fiscal management (through revised SGP, Flexibility clauses, and the EFSI), economic stimulus (through the EFSI), and financial stability (through the OMT and the “whatever it takes” speech).

## 2.2 *Did the Eurocrisis trigger a transforming cycle?*

Determining whether we are witnessing the early days of the final stage of transformation of the EU (or eventually, the beginning of its own undoing) is equally not trivial. While, in general, the institutional pattern seems to indicate –thanks to both the recent integration, and the path agreed in the Five Presidents’ report – that indeed we might be on the verge of a progressive transformation, political trends have also increased the likelihood of disintegration. Both outcomes, however, are legitimate effects of a transforming cycle. As discussed in Chapter 6, there is some evidence in support of the idea that the crisis intensity is connected with stronger preferences for integration in the fiscal field, in particular concerning the creation of Eurobonds and of an economic government of the EU. The evidence discussed in Chapter 6 is indeed suggestive, but unfortunately not conclusive: data availability is limited to the crisis period, and therefore useful to assess only the effect of crisis *intensity*, not of the crisis as such.

Albeit not conclusive, the evidence presented in Chapter 6 supports the view that the crisis had an effect on preferences for fiscal integration. However, many countries have by now passed the most critical phase, and the preferences for integration have therefore faded. In principle, this seems to suggest that the crisis was not able to trigger the beginning of a transformative cycle. However, in several countries the crisis has yet to be resolved, and the discourse concerning fiscal integration, although weakened today, has not yet disappeared. Moreover, there is evidence that the crisis has triggered politicization, both in the form of accrued authority of the central institutions (analyzed in detail in Chapter 4) and of increased negative politicization in the form of Euroscepticism (analyzed in Chapter 7). It is worth nothing that Chapter 7 only dealt with *extreme* Euroscepticism, as a potential source of the Union’s break-up. However, the effects of the crisis on *Soft* Euroscepticism are deemed to be even higher.

In sum, of the two elements which characterize a transforming cycle (integration of core state powers and politicization) the latter is clearly emerging in different forms, polarizing the discourse concerning the former, whose integration becomes therefore more troubled and disputed (again, as expected, given that integration of fiscal policy would constitute the transfer of a key element of sovereignty).

### 3. Theoretical insights

To some extent, the goal of this thesis was also to bring forward some fresh thinking concerning the fundamental pillars of functional integration theory. I believe that the theoretical contribution of this dissertation has been threefold.

First, the dissertation provides a clarified, simplified and streamlined framework to understand the functional integration dynamics. In general, Chapter 1 provides a coherent reconstruction of Neofunctionalism's fundamental pillars as they evolved over time. The “functional clock” and associated hypotheses, developed in the theoretical section of Chapter 4, help in clarifying the possible reactions to a given crisis-induced pressure to shift competences across tiers of government.

Second, through this thesis I contributed to enrich the scholarly understanding of the link between functional integration dynamics, theories of legitimacy, and the process of (negative) politicization. While the process of (negative) politicization has been mainly dealt with, conceptually, in the conclusive pages of Chapter 1, the precise connection between legitimacy crises (either “performance deficits” or “democratic deficits”) has been developed in the first part of Chapter 5. Theoretically speaking, Chapter 5 also contributes to further develop the “third trilemma”, perturbing the original setting proposed by Rodrik towards a model which could better capture the reality of European Integration. In this regard, the issue of the lack of shared identity has emerged as the leading element preventing the smooth transition towards a fiscal federation. A “theory of functional legitimacy” (indeed the title of one of the papers published as spillover of this dissertation) encompasses several of these elements, from politicization to identity. Indeed, the crisis-integration dynamics can also be read through the lenses of functional legitimacy theory, as done in figure 1 and 2 of Chapter 5.

Finally, the dissertation has also provided, especially through Chapter 2, an overall reshaping of the functional links between the different stages of European Integration. Chapter 3, although mostly empirical in nature, provides a useful set of three interdependent, nested trilemmas whose functional connections exemplify the cumulative logic postulated by Neofunctionalism.

#### 4. Policy implications

Although this thesis was mainly focusing on verifying, empirically, certain unsettled theoretical questions, I believe the results carry several policy implications as well.

First of all, in order to re-establish trust in the European integration process and therefore fight back Euroscepticism, actions need to be undertaken both in the short and in the long run. In the short run, the Union's performance deficit, and the fading output legitimacy, need to be addressed in order to interrupt the circular illness of the EMU. Only by re-establishing output legitimacy there will be sufficient consensus to overhaul the Union in the long run. This may require the introduction of a degree of fiscal integration in order to ease (although, not substitute) the adjustment process that southern member-states are bound to enact. However, as output legitimacy needs to be re-established *horizontally*, any centralized stabilization system should be carefully balanced in order to avoid fuelling the north-south divide and thus provoke a further rise of populism on either side of the cleavage; the introduction of policies tailoring structural unemployment and productivity growth may, in fact, be supported in both groups of countries.

Second, in the long run there is a clear functional need for establishing a new "grand bargain" between northern and southern member-states; the latter must accept a degree of control on domestic expenditure and economic policy in order to ensure debt sustainability and economic convergence; the former cannot refrain any longer from creating a substantially stronger central budget for the provision of common goods and of some central countercyclical policies. A clear way forward would be to centralize the provision of certain public goods which would be better provided at European level, thereby freeing resources at domestic level while achieving productivity and efficiency gains at European level. In addition, in order to ensure that domestic economic policy making does not take an excessively divergent path, a system of

incentives for reforms, along with a stronger scrutiny of economic policy, would clearly strengthen the EMU. Progressively, a system of incentives may evolve towards the creation of a true central budget, in line with the 2025 Five Presidents' Report. (In Nicoli 2016d, a spin-off of this dissertation, I detail the rationale, structure and timeline of a specific policy proposal, the Joint Budgetary Procedure).

In my view, the optimal way to organise the transition would require a twofold action plan. On the one hand, a clear set of "convergence criteria 2.0" should be set up; countries wishing to participate in the common Treasury should perform in line with the new criteria for a sufficiently long period of time in order to ensure real convergence. On the other hand, a contractual agreements' Fund could be set up to support the implementation of reforms needed domestically to ensure smooth convergence. Eventually, contributions received from the Fund would be non-refundable in case of successful convergence, but could be transformed in loans if the country fails to achieve convergence.

Third, in the long term, the EMU is in need to re-establish its input legitimacy. Therefore, it must address the issue of its central democratic governance, especially from the point it introduces common fiscal instruments onwards. While, in the short term, an enhanced supervision and scrutiny by national Parliaments may be the only way forward, it is clear to me that in the long run such a situation would not be sustainable, and only the European Parliament (or another, similar assembly) can provide true EU-wide Input Legitimacy. Transferring a formal fiscal competence to the European Parliament, however, requires to address the identity issue. Therefore, in order to ensure the success of its democratic governance in the future, the EMU needs to put in place instruments to foster the sense of shared identity as early as possible, possibly well in advance to the competences' transfer to the European Parliament. In fact, while political identities are not fixed and evolve over time, it is unlikely that they change or emerge overnight. Strengthening of the European Identity should therefore be a high priority for European policy makers, both as a tool to fight back Euroscepticism and populism, and to prepare the Europeans for a future of more interdependent, if not more integrated decisions on fiscal and economic matters.

## **5. Final remarks**

As stated above, this dissertation marks the beginning of a new development phase of my thinking about the future of Functional integration. Future research will take several parallel avenues to bring Functionalism forward both in empirical and theoretical terms. While parts of this dissertation have been published as stand-alone papers, I expect to reshape this work on a more cohesive and fluid volume, preparing it for publication as a book under the working title “*Unmanifested Destiny? Revisiting political Political Integration Conondrums in times of crisis*”. The book version of this thesis will also feature new research, aiming, in particular, to develop further the analysis of crisis-induced policies and to refine the empirical assessment of Euroscepticism. This volume—despite having contributed, hopefully, to solve some answers – opens in my view many new questions. Some are theoretical in nature and concern the modelling and the dynamics of the political transformation cycle; some are more empirical, and concern, especially, the role of polarization, politicization, and identities in this new phase of political integration. Finally, the most challenging questions address the strategies required to forge an agreement across member-states, along with the appropriate design of the reform of the Eurozone. In each of these fields, writing this dissertation offered me new insights and raised new questions, which I hope I will contribute to solve in the incoming years of research.





## Bibliography

- Acharya, V., Drechsler I. and P. Schnabl (2011). "A Pyrrhic Victory? Bank Bailouts and Sovereign Credit Risk." *Working Paper* No. 17136, National Bureau of Economic Research, June 2011
- Adam, K., Pei K. and A. Marcet (2012) House Price Booms and the Current Account. *NBER Macroeconomics Annual*, Vol 26 Issue 1.
- Agné H.(2007) The Myth of International Delegation: limits and suggestions for Democratic Theory in the context of the European Union". *Government and Opposition*, Vol. 42, No.1, pp 18-45
- Aguiar, M., Amador, M., Fahri, E. and G. Gopinath (2014) "Sovereign Debt Booms in Monetary Unions". *American Economic Review: papers and proceedings*, No. 104, Issue 5, pp. 101-106
- Akitoby, B. (eds) (2013) reassessing the role and modalities of fiscal policy in advanced economies. *International Monetary Fund Policy Paper*, June 2013.
- Alesina, A. and R Wacziarg (1999) "Is Europe Going Too Far?" *Carnegie-Rochester Conference Paper Series on Public Policy*, Vol. 51, pp. 1-42.
- Alt, J., Lassen D. and J. Wehner, (2012) Moral Hazard in an Economic Union Politics, Economics, and Fiscal Gimmickry in Europe. *Political Science and Political Economy Working Paper*, No. 05/2012, London School of Economics, Department of Government.
- Anderson, C. (1998) 'When in Doubt, Use Proxies: Attitudes Toward Domestic Politics and Support for European Integration'. *Comparative Political Studies* No.5, Vol.31, pp. 569-501
- Anderson, C. and K. Kaltenthaler (1996) 'The Dynamics of Public Opinion Toward European Integration, 1973-1993'. *European Journal of International Relations*, No.2, Vol.2, pp. 175-199

- Angeloni, I. and M. Ehrmann (2007) Euro Area Inflation Differentials. *The B.E. Journal of Economics*, Vol. 7, Issue 1, pp. 1-36
- Arghyrou, M. G. and J. Tsoukalas (2010 a) “The Option of Last Resort: a two-currency EMU”, *Roubini Global Economics Euromonitor*, 7 January 2010
- Arghyrou, M. G. and J. Tsoukalas (2010 b) “The Greek Debt Crisis: Likely Causes, Mechanics and Outcomes”. *Cardiff Economics Working Papers*, No. E2010/3
- Armington, K. and B. Ceka (2013) The loss of Trust in the European Union in the Great Recession since 2007: the role of heuristics from the national political system. *European Union Politics*, Vol. 15, Issue 1, pp. 82-107
- Arpaia, A. and K. Pichelmann (2007) Nominal and real wage flexibility in EMU. *European Economy, Economic Papers series* No.281
- Bakker, R., Edwards, E., Hooghe, L., Jolly, S., Marks, G., Polk, J., Rovny, J., Steenbergen, M., and M. Vachudova (2015) "2014 Chapel Hill Expert Survey: Version 2015.1." University of North Carolina, Chapel Hill.
- Balassa, S. (1961) *The theory of economic integration*. Richard D. Irwin, Homewood.
- Baldwin, R., Beck, T., Bénassy-Quéré, A., Blanchard, O., Corsetti, G., De Grauwe, P., Den Haan, W., Giavazzi, F., Gros, D., Kalemli-Ozcan, S., Micossi, S., Papaioannou, E., Pesenti, P., Pissarides, C., Tabellini G. and B. Weder di Mauro (2015) Rebooting the Eurozone, Step-1: Agreeing a common narrative. *CEPR Policy Insight*, No. 85, November 2015
- Banerji, A., Barkbu, B., John, J., Kinda, T., Saksonovs, S., Schoelermann, H. and T. Wu (2015), “Building a better union: Incentivizing Structural reforms in the euro area”, IMF Working Paper No.2015/15.
- Barbiero, F. and Z. Darvas (2014) In sickness and in Health: protecting and supporting public investment in Europe. *Bruegel Policy Contribution*, No. 02/2014.
- Bargaoanu, A., Radu, L. and E. Negrea-Basuioc (2014) ‘The rise of Euroscepticism in Time of Crisis: Evidence from the 2008-2013 Eurobarometers’. *Romanian Journal of Communication and Public Relations*, Vol. 16, Issue 1, pp. 25-40
- Barroso, J. M. (2011). *Speech by President Barroso at the Plenary Assembly of the European Parliament*.

Strasbourg, October 27<sup>th</sup>, 2011.

Basu, K. And J. Stiglitz, (2013) International Lending, Sovereign Debt and Joint Liability: and economic theory for amending the Treaty of Lisbon. *World Bank Policy Research Working Paper Series*, No. 6555, The World Bank

Bayoumi, T. and B. Eichengreen (1996a) Operationalising the Theory of Optimal Currency Areas. *CEPR Discussion Paper* no. 1484.

Bayoumi, T. and B. Eichengreen (1996b) “Ever closer to heaven? An optimum-currency-area index for European Countries.” *CIDER Working Paper Series*, No. 078-C96

Bayoumi, T. and B. Eichengreen (1998) Exchange Rate Volatility and Intervention: Implications of the Theory of Optimal Currency Areas. *Journal of International Economics*, Vol. 45, Issue 2, pp. 191-209

Beblavy M. and I. Maselli, (2015) The Case for an European Unemployment Benefit Scheme. *CEPS Commentary*, May 19<sup>th</sup>, 2015

Beblavy M., Maselli I. and G. Marconi (2015) A European Unemployment Benefit Scheme: rationale and challenges ahead. *CEPS Special Study* No. 119, September 2015.

Beetsma, R. and L. Bovenberg (2001) “Structural distortions and decentralized fiscal policies in the EMU”. *CEsifo Working Papers Series*, No.473

Beine, M., Candelon, B., and A. Hecq (2000) Assessing a perfect European Currency Area: a Common Cycles Approach. *Empirica*, Vol. 27, No. 2

Beirne, J. and M. Fratzscher (2013) “The pricing of sovereign risk and contagion during the European sovereign debt crisis. *Journal of International Money and Finance*, Vol. 34, Issue C, pp. 60-82.

Belke, A. (2012): Doomsday for the Euro Area: Causes, Variants and Consequences of Breakup. Working Paper, Bertelsmann Stiftung, Gütersloh.

Belke, A. and F. Venhoyer (2013) Doomsday for the Euro Area: Causes, Variants and Consequences of Breakup. *International Journal of Financial Studies*, Vol. 1, issue 1, pp. 1-15

Bellucci, P., Sanders, D., Toka, G. And M. Torcal (eds) (2012) *The Europeanisation of national politics? citizenship and support in a post-enlargement union*. Oxford University Press, Oxford, 2012.

Benassi-Quéré, A., Ragot, X. and G. Wolff (2015) Which Fiscal Union for the Euro Area? *Bruegel Policy*

*Contribution* No.05/2015.

Bénétrix, A. and P. Lane (2013) "Fiscal Cyclicalities in the EMU", *Journal of International Money and Finance*, Vol. 34, Issue C, pp. 164-176

Bergin, P. (2000) "Fiscal Solvency and Price Level Determination in a Monetary Union". *Journal of Monetary Economics*, Vol. 34, Issue 1, pp. 37-53

Bertoncini, Y. and N. Koenig (2014) Euroscepticism or Europhobia: voice vs. exit? *Notre Europe Policy Paper* No.121.

Betchel, M., Hainmueller, J. and Y. Margalit (2014) "Preferences for International Redistribution: the Divide over the Eurozone Bailouts". *American Journal of Political Science*, Vol. 58, Issue 4, pp. 835-856

Bodin, J. (1576) *Les Six Livres de la République*. Bordeaux, Confluences, 1999.

Bofinger, P. (2015) German wage moderation and the Eurozone crisis. *Social Europe*, December 1st, 2015

Bofinger, P., Feld, L., Franz, W., Schmidt, C. and B. Weder di Mauro (2011) A European Redemption Pact. *Annual Economic Report 2011/2012*, German Council of Economic Experts.

Böll, S. and K. Von Hammerstein (2012) Interview with Finance Minister Schäuble, part 2: The Most Important Thing Is a Fiscal Union'. *Der Spiegel*, June 25, 2012.

Bonatti, L. (2014) *Verso un meccanismo europeo di "accordi contrattuali": partnerships per la crescita e l'occupazione*. Chapter in: Paganetto, L. (ed.) (2014) *Revitalizing Anemic Europe: Rapporto del Gruppo dei 20 al Governo Italiano*. Roma, Eurilink.

Bonatti, L. and A. Fracasso (2013) The German Model and the European Crisis. *Journal of Common Market Studies*, Vol. 51, No. 6

Bordo, M.D., Jonung, L. and A. Markiewicz (2011) Does the Euro need a fiscal union? Some lessons from history. *NBER Working Paper* No. 17380

Boter, S., Caffet, J.C., and V. D. Martin (2011) Low Labour Mobility is more than ever an obstacle to Euro-Zone cohesion. *Flash Economics* No.24

Brauninger, D. and C. Majovsky (2011) Labour Mobility in the Euro Area. *Reports on European Integration-EU monitor* No. 85. Deutsche Bank Research

Brunkhorst, H. (2005) *Solidarity: From Civic Friendship to a Global Legal Community*. MIT Press,

Cambridge

Bruno, M. and J. Sachs, (1985) *Economics of Worldwide Stagflation*. Oxford, Oxford University Press

Bruter, M. (2003) Winning hearts and minds for Europe: the impact of news and symbols on civic and cultural European Identity. *Comparative Political Studies*, Vol. 36, No. 10, p. 1148-1179

Bryde, B. O. (1994): Die bundesrepublikanische Volksdemokratie als Irrweg der Demokratietheorie. *Staatswissenschaften und Staatspraxis: rechts-, wirtschafts- und sozialwissenschaftliche Beiträge zum staatlichen Handeln*. Vol. 5, Issue 3, pp. 305-330.

Buiter, W., Corsetti, G. and P. Pesenti (1998) Interpreting the ERM crisis: Country-specific and systemic crises. *Princeton Studies in International Finance*, No. 84.

Bundesverfassungsgericht (1993): "Maastricht case", Cases 2134/92 & 2159/92, Decision of October 12, 1993.

Bundesverfassungsgericht (2009): "Lisbon case", Case 02/08, Decision of June 30, 2009.

Bundesverfassungsgericht (2012): "ESM case", Case 1390/12, Decision of September 12, 2012.

Buti, M. and A. Sapir (1998) "Economic Policy in the EMU". *ULB Institutional Repository*.

Camera dei Deputati, 2014. *Atto di Indirizzo*, March 7th, 2014

Cameron, D. (2013) *Speech of the Prime Minister on the future of the British-EU relations*, 23 January 2013.

Castelli Gattinara, P. and C. Froio (2014) *Opposition in the EU and opposition to the EU: soft and hard Euroscepticism in Italy in the time of austerity*. Chapter in: Institute of European Democrats (eds) (2014) *Rising Populism and the European Elections*. IED, Brussels, Spring 2014

Charlemagne (column), 2014. "Your Flexible Friend". *The Economist*, March 14th, 2014

Christiansen, T. (1996) "A Maturing Bureaucracy? The Role of the Commission in the Policy Process" in Richardson, J. (ed.) *European Union Power and Policy-Making*, London and New York: Routledge, pp. 77-95.

Christiansen, T. (2001) "The European Commission: Administration in Turbulent Times", in Richardson, J. (ed.) *European Union: Power and Policy Making*, 2nd Edition, London-New York: Routledge: 95-114

- Christiansen, T., Jorgensen, K. E. and A. Wiener (1999) The Social Construction of Europe. *Journal of European Public Policy*, Vol. 6, issue 4, pp. 528-544
- Claeys, G., Darvas, Z., and G. Wolff (2014) Benefits and Drawbacks of a European Unemployment Insurance. *Bruegel Policy Brief*, No. 6/2014
- Closa, C. and A. Maatsch, (2013) In a Spirit of Solidarity? Justifying the European Financial Stability Facility (EFSF) in national parliaments' debates. *Journal of Common Market Studies*, Vol. 52, No. 4, pp. 826-842
- Cohon, R. (2001) The Shackles of Virtue: Hume on Allegiance to Government. *History of Philosophy Quarterly*, No. 18, Issue 4, pp. 393-413
- Cohon, R. (2010) "Hume's Moral Philosophy". In Zalta, E. (eds) (2010) *The Stanford Encyclopedia of Philosophy*, Fall 2010.
- Collignon, S. (2011) The Governance of European Public Goods. Chapter in Tarschys, D. (ed.) (2011) *The EU Budget: what should go in? What should go out?* Stockholm: SIEPS.
- Cottarelli, C. and M. Guerguil (eds) (2015) *Designing a European Fiscal Union: Lessons from the experience of fiscal federations*. New York: Routledge.
- Crum, B. (2013) Saving the Euro at the Cost of Democracy? *Journal of Common Market Studies*, Vol. 51, Issue 4, pp. 614-630.
- D'Apice, P. (2015) Cross-Border Flows Operated Through the EU Budget: an overview. *European Economy Discussion Papers*, December 2015.
- Damonte, A. (2008). European Integration as Rodrik Trilemma. *Working Paper Series* no. 10/08, Università degli Studi di Milano
- Daniel, B. and C. Shiamptanis (2013) "Pushing the limit? Fiscal Policy in the European Monetary Union". *Journal of Economic Dynamics and Control*, Vol. 37, Issue 11, pp. 2307-2321
- Daniele, G. and B. Geys (2014) Public support for European Fiscal Integration in times of crisis. *Journal of European Public Policy*, vol.22, issue 5, pp. 650-670.
- Dao, M., Furceri, D. and P. Loungani (2013), Regional labour market adjustments in the US and Europe, *IMF Working Paper*
- Darpmann, S. (2009) Solidarity and Cosmopolitanism. *Ethic Theory and Moral Practice*, Issue 12, pp. 303-

315

Darvas, Z. (2012) “Intra-Euro Rebalancing is inevitable, but insufficient”. *Bruegel Policy Contribution*, Issue No.15, August 2012

Darvas, Z. (2012) Compositional Effects on Productivity, Labour Cost and Export Adjustment. *Bruegel Policy Contribution*, Issue 11/2012, June 2012

De Cillia, R., Reisigl, M. and R. Wodak (1999) The Discursive Construction of National Identities. *Discourse and Society*, Vol. 10, No. 2 pp.149-173

De Finance, S., (2014) A “traffic-light” approach to the implementation of the 2011-2012 country-specific Recommendations. *European Parliament Study*, March 2014.

De Grauwe, P. (1998). The Euro and the Financial Crises. *Financial Times*, 20/02/1998

De Grauwe, P. (2007) “*Economics of Monetary Union*”, Oxford University Press, 2007 Italian Edition

De Grauwe, P. (2010) Why a tougher Stability and Growth Pact is a bad idea. *VoxEU contribution*, 4 October 2010

De Grauwe, P. (2011a) Governance of a Fragile Eurozone. *CEPS working document*, No. 346/May 2011

De Grauwe, P. (2011b) The European Central Bank as a lender of last resort. *VoxEU contribution*, 18 August 2011

De Grauwe, P. (2012a) *Economics of Monetary Unions*. Oxford: Oxford University Press.

De Grauwe, P. (2012b) In Search of Symmetry in the Eurozone. *CEPS Policy Briefs* No. 268

De Grauwe, P. (2012c) The Governance of a fragile Eurozone. *Australian Economic Review*, Vol. 45, Issue 3, pp. 255-268

De Grauwe, P. (2013) Design Failures in the Euro Area: Can they be fixed? *European Economy, Economic Papers* No.491/April 2013

De Grauwe, P. and F. P. Mongelli (2005) Endogeneity of Optimal Currency Areas: what bring countries sharing a single currency closer together? *ECB Working Paper Series*, No. 468

De Grauwe, P. and Y. Ji (2012) Mispricing of Sovereign Risk and Macroeconomic Stability in the Eurozone. *Journal of Common Market Studies*, Vol. 50, Issue 6, pp. 866-880

De Grauwe, P. and Y. Ji (2013a) Selffulfilling crises in the Eurozone: an empirical test. *Journal of*



*International Money and Finance*, Vol. 34, April 2013, pp. 15-36

De Grauwe, P. and Y. Ji (2013b) Fiscal implications of ECB's bond buying programme. *VoxEU contribution*, June 14 2013.

De Grauwe, P. and Y. Ji (2013c) More Evidence that Financial Markets Imposed Excessive Austerity in the Eurozone. *CEPS Commentaries*, February 2013

De Wilde, P., Michailidu, A. and H.-J. Trenz (2014) 'Converging on Euroscepticism: Online Polity Contestation During European Parliament Elections'. *European Journal of Political Research*, January 2014.

De Witte, F. and M. Hartmann (2013) 'Ending the Honeymoon: constructing Europe Beyond the Market'. *German Law Journal*, Vol.14, No.05, p.449-452

Dekavalla, M. (2010) Tax, War and Waiting lists: the construction of national identity in newspaper coverage of general elections after devolution. *Discourse and Society*, vol. 21, No. 6, pp. 638-654

DeLong, J. B., and L. Summers (2012) Fiscal Policy in a depressed economy. *Brookings Papers on Economic Activity*, Spring 2012

Delpla, J. and J. von Weizsäcker, (2010). The Blue Bond Proposal, *Bruegel Policy Brief*, Issue 03/2010

Delpla, J. and J. von Weizsäcker, (2011). Eurobonds: the blue bonds concept and its implications. *Bruegel Policy Contribution*, Issue 02/2011.

Deo, S., Donovan, P. and L. Hathaway (2011): Euro Break-Up – The Consequences. *Global Economic Perspectives*, UBS Investment Research Department, London.

Deroose, S., Hodson, D. and J. Kuhlmann (2008) the Broad Economic Policy Guidelines: Before and after the Re-Launch of the Lisbon Strategy. *Journal of Common Market Studies*, Vol.49, Issue 4.

Dhéret, C., Martinovici, A. and F. Zuleeg (2012) The State of Play on the EU Multiannual Financial Framework (MFF) 2014-2020 interinstitutional negotiations. EPC report for the Committee of Regions, pp. 29-30.

Dhéret, C., Pascouau, Y., Lazarowich, A. and F. Nicoli (2013) Completing the Single European Labour Market. *EPC Issue Paper*, May 2013

Dobbs, C. and M. Spence (2012) Preventing an Eurozone Bank and Bond Run. *Vox Policy Portal*, June

15th, 2012

Dobrescu, P. and F. Durach (2014) Euroscepticism- A sign of Europe in distress. *Romanian Journal of Communication and Public Relations*, Vol. 16, Issue 1

Dorrucci, E., Ioannou, D., Mongelli, F. P. and A Terzi (2015), "The Four Unions "PIE" on the Monetary Union "cherry": A New Index of European Institutional Integration", ECB Occasional Paper No. 160

Dowd, B., (1982) The logic of moral hazard: a game-theoretical illustration. *The Journal of Risk and Insurance*, Vol.49, No. 3, pp.443-447

Dowd, K., (2009), Moral Hazard and the Financial Crisis. *Cato Journal*, No. 29, vol. 1

Draghi, M., (2015a), Stability and Prosperity in the Monetary Union. *Project Syndicate*, 2nd January, 2015

Drudi, F., Durré, A. and F.P. Mongelli (2012). The Interplay of Economic Reforms and Monetary Policy: The Case of the Eurozone, *Journal of Common Market Studies*, Vo. 50, Issue 6, pp.881-898

Durkheim, E., (1893) *De la division du travail social*, Paris, Félix Alcan. Available for download at [http://classiques.uqac.ca/classiques/Durkheim\\_emile/division\\_du\\_travail/division\\_travail.html](http://classiques.uqac.ca/classiques/Durkheim_emile/division_du_travail/division_travail.html)

Dymski, G. (2013) The Eurozone Crisis as a Trilemma Forcefield: Fleming, Mundell, and Power in Finance. *Working Paper*, University of Leeds

European Commission - Directorate General for Economic and Financial Affairs (1990) "One Market, One money: an evaluation of the potential benefits and costs of forming an economic and monetary union". *European Economy*, No. 44

European Commission (2015): Eurobarometer 77.3 (2012). TNS Opinion,, Brussels

European Commission (2013) Public Opinion in the European Union. Standard European Barometer 80, December 2013

European Commission (2014): Eurobarometer 75.3 (2011). TNS Opinion, Brussels

European Commission (2014): Eurobarometer 76.3 (2011). TNS Opinion, Brussels

European Commission, Brussels (2014): Eurobarometer 80.1 (2013). TNS Opinion, Brussels

European Commission, Brussels (2015): Eurobarometer 78.1 (2012). TNS opinion, Brussels

European Commission, Brussels (2015): Eurobarometer 81.4 (2014). TNS Opinion, Brussels

European Commission, Brussels (2015): Eurobarometer 82.3 (2014). TNS Opinion, Brussels

- European Commission, Brussels (2015): Eurobarometer 83.3 (2015). TNS Opinion, Brussels
- European Commission, Brussels (2016): Eurobarometer 79.3 (2013). TNS Opinion, Brussels
- European Commission, Brussels (2016): Eurobarometer 84.3 (2015). TNS opinion, Brussels
- Economides, G., Kalyvitis, S. and A. Philippopoulos (2008) Do Foreign Aid Transfers Distort Incentives and Hurt Growth? Theory and Evidence from 75 Aid-recipient Countries. *Public Choice*, Vol. 134, Issue 3, pp. 463-488
- Eichenberg, R. C. and R. Dalton (2007) Post-Maastricht Blues: the transformation of citizens support for European integration, 1973-2004. *Acta Politica*, No. 42, 2007, pp. 128-52
- Eichengreen, B. (2008) The breakup of the Euro Area. *NBER working Paper* No. 11393
- Eichengreen, B. and C. Wyplosz (1998) "The Stability Pact: More than a minor nuisance?" *Economic Policy*, No. 13, Issue 26, pp. 65-113
- Eichengreen, B. and J. Von Hagen (1996) "Federalism, Fiscal Restraints, and European Monetary Union" *American Economic Review*, Vol. 86, Issue 2, pp. 134-138
- Enderlein, E. and J. Haas (2015) What would a European Finance Minister do? A proposal. *Jacques Delors Institute Policy Paper* No. 145.
- Enderlein, H. and J. Haas (2015) What would a European Financial Minister do? A proposal. *Jacques Delors Institute Policy Paper*, No.145- October 2015
- Enderlein, H., Bofinger, P., Boone, L., De Grauwe, P., Piris, J.C., Pisani-Ferry, J., Rodrigues, M. J., Sapir, A. and A. Vitorino (2012) Completing the Euro: a roadmap towards a fiscal union in Europe. *Report of the Tommaso Padoa Schioppa Group*, Notre Europe, Paris.
- Enders, Z., Jung, P. and G. Müller (2013) "Has the Euro changed the business cycle?" *European Economic Review*, Vol. 59, Issue C, pp. 189-211
- Eschner, B., Pfetsch, B. and A. Silke (2008) The contribution of the press to Europeanization of public debates: a comparative study of issue salience and conflict lines of European integration. *Journalism*, Vol.9, issue 4
- Etzioni, A. (2001) *Political Unification Revisited*. Lexington Books, Boston
- Eyraud, L. and T. Wu (2015) Playing by the rules: reforming fiscal governance in Europe. *International*

*Monetary Fund Working Paper*, No. 15/67, Washington

Fabbrini, S. (2014) Intergovernmentalism and its outcomes: the implications of the Eurocrisis on the European Union. *Working Paper Series*, Luiss School of Governance.

Fabbrini, S. (2015) *Which European Union? Europe after the Eurocrisis*. Cambridge: Cambridge University Press.

Fama, E. (1965) The behavior of stock-market prices. *The Journal of Business*, Vol. 38, No. 1

Farage, N. (2014) Intervention in the European Parliament Plenary, October 22th, 2014, Strasbourg.

Farhi, E. and I. Werning (2012) Dealing with the Trilemma: Optimal Capital Controls with Fixed Exchange Rates. NBER Working Paper No. 18199

Farhi, E. and I. Werning (2012) Fiscal Unions. NBER Working Paper No. 18280

Farhi, E. and J. Tirole (2014) Deadly Embrace: Sovereign and Financial Balance Sheets Doom Loops. Harvard University Working Paper, November 2014.

Fauri, F. (2006) *L'integrazione economica europea 1947-2006*, Il Mulino, Bologna

Fedeli, S., Forte, F. and O. Ricchi (2013) The Long Term Negative Relationship between Public Deficit and Structural Unemployment: an empirical study of OECD Countries (1980-2009). *Atlantic Economic Journal*, Vol. 43, Issue 1, pp. 39-54.

Ferrer, J. N., Le Cacheux, J., Benedetto, G. and M. Saunier (2016) Study on the Potential and Limitation of Reforming the Financing of the EU Budget. *European Commission Study*, June 2016.

Fioretos, O. (2011) Historical Institutionalism in International Relations. *International Organization* No. 65, pp. 367-399

Fisher, J. (2000). From confederacy to federation. Thoughts on the finality of European Integration. Berlin, Humboldt University, 12 May 2000.

Fitzgibbon, J. (2013) Citizens Against Europe? Civil society and Eurosceptic Protest in Ireland, United Kingdom and Denmark. *Journal of Common Market Studies*, Vol. 51, Issue 1, pp. 105-121

Flora, P., Kuhnle, S. and D. Urwin (eds) (1999) *'State Formation, Nation-Building and Mass Politics in Europe: the Theory of Stein Rokkan.'* Oxford: Oxford University Press

Follesdal, A and S. Hix (2006): Why there is a Democratic Deficit in the EU: A Response to Majone and Moravcsik. *Journal of Common Market Studies* 44 (3), pp. 533-562

- Frankel, J. A. and A. K. Rose (1998) "The endogeneity of the Optimal Currency Area criteria". *The Economic Journal*, Vol. 108, No. 449, pp. 1009-1025
- Friedrich, D. and S. Kroger (2013): Democratic Representation in the EU: Two Kinds of Subjectivity. *Journal of European Public Policy* 20 (2), pp. 171-189
- Gabel, M. (1998) Public Support for European Integration: an Empirical Test of Five Theories. *Journal of Politics*, No. 60, pp. 333-354
- Gabel, M. and H. D. Palmer (1995) Understanding variation in public support for European Integration. *European Journal of Political Research*, Vol. 27, Issue 1 pp. 3-19.
- Geherels, F. and B. Johnston (1955) "The economic gains of European integration", *Journal of Political Economy*, Vol.63, No.4
- Genschel, P. and M. Jachtenfuchs (2016) "More Integration, Less Federation: the European Integration of Core State Powers". *Journal of European Public Policy*, No.23, Issue 1, pp. 42-59.
- Giavazzi, F. and O. Blanchard (2002) Current Account Deficits in the Euro Area. The end of the Feldstein Horioka puzzle? *Brookings papers*, September 2002
- Gomez, R. (2014) The Economics Strikes Back: support for the EU during the great recession. *Journal of Common Market Studies*, Vol.53, Issue 3, pp.577-592
- Gould, C. (2007) Transnational Solidarities. *Journal of Social Philosophy*, Vol. 38, No.1, pp- 148-164
- Gratschew, M. (2004) "Compulsory Voting in Western Europe". Chapter in: Gratschew, M. and L. R. Pintor (eds) (2004) *Voter Turnout in Western Europe*. International IDEA, Stockholm, 2004.
- Grimm, D.(1995) Does Europe Need a Constitution? *European Law Journal* 1 (3), pp. 282-302
- Grimm, R. (2015) The Rise of the German Eurosceptic Party Alternative für Deutschland, Between Ordoliberal Critique and Popular Anxiety. *International Political Science Review*, Vol. 36, No. 3, pp. 264-278
- Gros, D. (2012) "Macroeconomic Imbalances in the Euro Area: Symptom or Cause of the Crisis?" *CEPS Policy Briefs* No. 266, April 2012.
- Gros, D. (2014) Investment as a key to recovery in the Euro Area? *CEPS Policy Brief* No. 326
- Gros, D. and D. Schoenmaker (2014) "European Deposit Insurance and Resolution in the Banking Union".

*Journal of Common Market Studies*, Volume 52, Issue 3, pp. 529-546

Guyon, T. (2007) "Should we worry about current account imbalances in a monetary union?" *Trésor-Economics*, No. 20, October 2007

Haas E.B. and P. Schmitter (1964) "Economics and Differential patterns of Political Integration: projections about Unity in Latin America". *International Organization* Vol. 18. pp. 705-737

Haas, E. B. (1964): *Beyond the Nation State. Functionalism and International Organization*. European Consortium for Political Research, 2008.

Haas, E. B. (2003) "Introduction: Institutionalism or constructivism?". Introduction to the 2004 edition of: Haas, E.B. (1958) *The Uniting of Europe. Political, Social and Economic Forces, 1950-1957*. 2004, University of Notre Dame Press

Haas, E.B. (1975) *The Obsolescence of Regional Integration Theory*. Berkley-Institute of International Studies

Habermas, J. (2011): Europe's Post-Democratic Era. *The Guardian*, November 10, 2011.

Habermas J. (2013), Democracy, Solidarity and the European Crisis. *Guest Lecture*, University of Leuven, April 26th, 2013.

Hallerberg, M., Marzinotto, B., and G. Wolff (2012) An Assessment of the European Semester. *Study*, Directorate for Internal Policies, European Parliament

Harmsen, R. and M. Spiering (eds) (2004) *Euroscepticism: Party Politics, National Identities and European Integration*. Editions Rodopi, Amsterdam

Hartmann, M. and F. De Witte (2013) Ending the Honeymoon: constructing Europe Beyond the Market. *German Law Journal*, Vol.14, No.05, p.445

Hausman, J. and W. E. Taylor (1981) Panel Data and Unobservable Individual Effects. *Econometrica*, Vol. 49, No. 6, pp. 1377-1398

Hefftlar, C. and W. Wessels (2013) The Democratic Legitimacy of the EU Economic Governance and National Parliaments, *IAI Working Papers*, No 13/2013

Henning, R. and M. Kessler (2012) Fiscal Federalism: US' History for architects of Europe's fiscal union. *Bruegel Essays and Lectures Series*, Brussels.

- Hernandez, E. and H. Kriesi (2015) The electoral consequences of the financial and economic crisis in Europe. *European Journal of Political Research*, Vol.55, issue 2, pp. 203-224
- Hix, S. (1998): Elections, Parties and Institutional Design: A Comparative Perspective on European Democracy. *Western European Politics* 3 (21), pp. 19-52
- Hix, S. (2007) Euroscepticism as anti-centralization: a rational-choice institutional perspective. *European Union Politics*, No. 8, issue 1, pp. 131-150
- Hix, S. (2008) Towards a partisan theory of EU politics. *Journal of European Public Policy*, No. 15, Issue 8, pp. 1254-1265.
- Hix, S. (2013) Why the 2014 European Elections Matter: Ten Key Votes in the 2009–2013 European Parliament. *European Policy Analysis*, No. 15/2013.
- Hix, S. and B. Høyland (2013) Empowerment of the European Parliament. *Annual Review of Political Science*, No. 16, pp. 171-189
- Hix, S. and M. Marsh (2011) Second-order effects plus pan-European political swings: An analysis of European Parliament elections across time. *Electoral Studies*, No. 30, pp. 4-15
- Hix, S. , Noury, A. and G. Roland (2006) Dimensions of Politics in the European Parliament. *American Journal of Political Science*, No. 50, Issue 2, pp. 494-511
- Hix, S. Noury, A. and G. Roland (2007) *Democratic Politics in the European Parliament*. Cambridge: Cambridge University Press, UK
- Hobolt, S. (2014) Ever closer or ever wider? Public attitudes towards further enlargement and integration in the European Union. *Journal of European Public Policy*, 21 (5). 664-680.
- Hobolt, S. and C. Wratil (2015) Public Opinion and the Crisis: the dynamics of support for the Euro. *Journal of European Public Policy*, vol. 22, No.2, pp. 238-256.
- Hobolt, S. B. and J.-J. Spoon (2012). Motivating the European voter: parties, issues, campaigns in European Parliament elections. *European Journal of Political Research*, No. 51
- Holinski, N., Kool, C. And J. Muysken (2012) “Persistent Macroeconomic Imbalances in the Euro Area: Causes and Consequences”. *Review of the Federal Bank of St. Luis*, Issue 1/2012, pp. 1-20
- Holland, D. And J. Portes (2012) Self-defeating austerity? *National Institute Economic Review*, Vol.222,

No. 1

Holló, D., Kremer, M. and M. Lo Duca (2012) CISS- A composite indicator of systemic stress in the financial system. *ECB Working Paper Series*, No. 1426

Hooghe, L. and G. Marks (2005) Calculation, community and cues public opinion on European integration. *European Union Politics*, Vol. 6, No. 4, pp. 419-433

Hooghe, L. and G. Marks (2009) A Postfunctionalist theory of European Integration: from permissive consensus to constraining dissensus. *British Journal of Political Science*, Vol. 39, Issue 1, pp. 1-23.

Howarth, D. and L. Quaglia (2013) “Banking Union as the Holy Grail: Rebuilding the Single Market in Financial Services, Stabilizing Europe's Banks and ‘Completing’ Economic and Monetary Union”. *Journal of Common Market Studies*, Vol. 51, Supplement Issue 1, pp. 103-123

In t Veld, J. (2007) The Potential Impact of the Fiscal Transfers under the EU Cohesion Policy Programme. *European Economy*, No.283

INET Council on Eurozone Crisis (2012) *Breaking the deadlock: a path out of the crisis*. Report of the Council, Institute for New Economic Thinking.

International Monetary Fund (eds) (1988) Policy Coordination in the European Monetary System. *IMF Occasional Paper* No. 61

Ioannou, D. and A. Niemann (2015) European economic integration in times of crisis: a case of Neofunctionalism? *Journal of European Public Policy*, Vol. 22, Issue 2, pp. 196-218

Ioannou, D. and L. Sacca (2011) Have Euro Area and EU economic governance worked? Just the facts. *ECB Working paper series*, No 1344/2011

Ioannou, D., Jamet, J. F. and and J. Kleibl (2015) Spillovers and Euroscepticism, *Working Paper Series* No.1815, European Central Bank

Isiksel, T. (2016) *Europe's Functional Constitution: a theory of Constitutionalism beyond the State*. Oxford: Oxford University Press.

Italian Government (2015) completing and strengthening the EMU. *Italian Contribution to the Five Presidents' Report*, May 2015.

Jaumotte, F. and P. Sodsriwiboon (2010) “Current Account Imbalances in the Southern Euro Area”.



*International Monetary Fund Working Paper*, wp/10/139

Jones, G. (2016) Italy's Renzi says budget flexibility was condition of Juncker's appointment. *Reuters*, Jan. 26th, 2016.

Juncker, J. C. (ed) (2015) *The Five Presidents' Report: Completing Europe's Economic and Monetary Union*.

Juncker, J. C. (2014a). *Speech by President Juncker at the European Parliament Plenary Session*, Strasbourg, July 15th, 2014

Juncker, J. C. (2014b). "Time for Action". *Speech by President Juncker at the European Parliament Plenary Session*. Strasbourg, October 22th, 2014

Juncker, J. C. (2015a) "State of the Union 2015: time for honesty, unity and solidarity". *Speech by President Juncker at the European Parliament Plenary Session*, Strasbourg, September 9th, 2015

Juncker, J. C. (2015b). *Speech by President Juncker at the European Parliament Plenary Session*, Strasbourg, October 27th, 2015

Juncker, J. C. (2016) The European Union: a source of stability in a times of crisis. *14th Norbert Schmelzer Lecture*, The Hague, March 3rd 2016

Kaldor, N. (1971). The Economic Effects of the Common Market. *The New Stateman*, 12 March 1971

Kam, C. and R. Franzese (2007) *Modelling and Interpreting Interactive Hypotheses in Regression Analysis*. Chicago: University of Michigan Press.

Kaminsky and C: Reinhart (1999) The Twin Crises: The Causes of Banking and Balance-of-payment Problems. *American Economic Review*, Vol. 89, No. 3

Karagiannis, Y. and M. Guidi (2014) Institutional change and continuity in the European Union: the super-Commissioner saga. *Acta Politica*, Vol. 49 Issue 2, pp- 174-195

Kawai, M. And S. Akiyama (2003): Implications of the Currency Crisis for Exchange Rates Arrangements in Emerging East Asia. *World Bank Policy Research Working Paper*. No. 2502

Kenen, P. (1969) "The Theory of Optimum Currency Areas: An Eclectic View," in Robert Mundell and Alexander Swoboda (eds), *Monetary Problems of the International Economy*, Chicago: University of Chicago Press (1969), pp.41-60.

- Keohane, R. O. (1984) *After hegemony: cooperation and discord in the world political economy*. Princeton: Princeton University Press
- Kielmansegg, P. G. (1994) Läßt sich die Europäische Gemeinschaft demokratisch verfassen? *Europäische Rundschau* 22 (2), pp. 23-33
- Kielmansegg, P. G. (1996) Integration und Demokratie. In Jachtenfuchs, Markus/Kohler-Koch, Beate. (eds) (1996): *Europäische Integration*, Lesk+Budrich, Opladen, pp. 47-71.
- Kierkegaard, J. (2015) Economic Governance Structures in the United States. *European Parliament Report*, October 2015
- King, T. (1999) *The European Commission: administration or government?* London: Centre for Policy Studies.
- Knedlik, T. and G. Von Schweinitz (2012) "Macroeconomic Imbalances as Indicators For Debt Crises in Europe". *Journal of Common Market Studies*, Vol. 50, Issue 5, pp. 726-745
- Kontochristou, M. and E. Mascha (2014) The Euro Crisis and the Question of Solidarity in the European Union: Disclosures and Manifestations in the European Press. *Review of European Studies*, Vol. 6, No. 2
- Koo, R. (2011) The world in Balance Sheet recession. Causes, Cure, and Politics. *Real World Economic Review*, Issue No. 58.
- Kopits G. and S. Symanky (1998) Fiscal Policy Rules, *International Monetary Fund Occasional Papers*, No. 162, Washington
- Krastev, I. (2012) The political logic of disintegration: seven lessons from the Soviet Union. *CEPS Essays*, Brussels, 2012.
- Kröger, S. and D. Fridrich (2013) Democratic representation in the EU: two kinds of subjectivity. *Journal of European Public Policy*, Nr. 20, Issue 2, p.171-189
- Krugman, P. (1991) Increasing Returns and Economic Geography. *Journal of Political Economy*, Issue 99, pp. 843-499
- Krugman, P. (1993) Inequality and the political economy of Eurosclerosis. *CEPR discussion papers*, No. 867.
- Krugman, P. (2012) "Europe's Austerity madness". *New York Times*, September 27th, 2012.
- Krugman, P. (2013) "Cyprus, Seriously". *New York Times*, March 26th, 2013

- Krugman, P. and A. J. Venables (1996) "Integration, Specialization and Adjustment". *European Economic Review*, Vol. 40, pp. 959-967
- Kuhn, T. and Stoeckel, F. (2014) 'When European integration becomes costly: the eurocrisis and public support for European economic governance', *Journal of European Public Policy* 21(4): 624-41.
- L'Angevin, C. (2007) Labour Market Adjustment Dynamics and Labour Mobility Within the Euro Area. *Documents du travail de la Direction Générale du Trésor et de la Politique économique*, No.06/ September 2007
- Lacombe, C. and F. Lemaitre (2012) Interview with Jens Weidmann. *Le Monde*, February 25th, 2012.
- Lane, P. R. and Milesi-Ferretti, G.M. (2012) "External Adjustment and the Global Crisis". *Journal of International Economics* No. 88, Issue 2, pp. 252-265.
- Lebrun, I. and E. Perez (2011) Real Unit Labour Costs Differentials in EMU: how big, how benign, and how reversible? *IMF Working Paper No. 109/2011*
- Lindberg, L.N. (1963) "*The Political Dynamics of European Economic Integration*" Stanford: Stanford University Press
- Lipset, M. and S. Rokkan (eds) (1967) '*Party Systems and Voting Alignments: cross-national perspectives*'. New York:Free Press
- Loth, W. (2013) Negotiating the Maastricht Treaty. *Journal of European Integration History*, Issue 19, No. 1
- Ludlow, P. (2013) European Integration in the 80s: in the way to Maastricht? *Journal of European Integration History*, Issue 19, No. 1
- MacIntyre, A. (1981) *After Virtue: A Study in Moral Theory*. University of Notre Dame press, Third Edition, 2007.
- MacNamara, K. (2002): Rational Fictions: Central Bank Independence and the Social Logic of Delegation. *West European Politics* 25 (1), pp. 47-76
- Mahoney, J. (2000) Path dependence in historical sociology. *Theory and Society*, No 29, pp. 507-548.
- Mahoney, J. And K. Thelen (eds). (2010) *Explaining Institutional Change*. Cambridge: Cambridge University Press.
- Majone, G. (1997) The regulatory state and its legitimacy problems. *Western European Politics*, No. 22,

Issue 1, pp. 1-24

Majone, G. (2001) Regulatory Legitimacy in the United States and the European Union. In Nicolaidis, K. and R. Howse (eds) (2001), *The Federal Vision: Legitimacy and Levels of Governance in the United States and the European Union*. Oxford: Oxford University Press, p.225-26.

Majone, G. (2014): From a Regulatory State to a Democratic Default. *Journal of Common Market Studies* 52 (6), pp. 1216-1223

Marzinotto, B. (2010) Two Crises, Two Responses. *Bruegel Policy Contribution*, Issue No. 1, 2010

Marzinotto, B., Sapir, A. and G. Wolff (2011) What kind of Fiscal Union? *Bruegel Policy Brief*, Issue 6, November 2011

Mayes D. G. and M. Virens (2002) Asymmetry and the problem of aggregation in the Euro Area. *Empirica*, Vol. 29, No. 1

McDougall, D. (ed.) (1977) *Report of the Study Group on the Role of Public Finance in European Integration*. Brussels, April 1977.

McKinnon (1973) On securing a Common Monetary Policy in Europe," *Banca Nazionale del Lavoro Quarterly Review*, March 1973.

McLaren, L. (2006) *Identity, Interests and Attitudes to European Integration*. Palgrave Macmillan.

Meade, J. E. (1957) The Balance-of-Payments problems of a European Free-Trade Area. *The Economic Journal*, Vol. 67, No. 267 (Sep., 1957), pp. 379-396

Meijers, M. (2013) The Euro-Crisis as a catalyst of the Europeanization of public spheres? A cross-temporal study of the Netherlands and Germany. *LEQS Papers No. 62/2013*, London School of Economics

Melitz, J. (2014) Why Europe needs two Euros, not one. *Vox Policy Portal*, July the 2nd, 2014

Ménéndez, A. J. (2000) "Another View of Democratic Deficit: No Taxation without Representation". In Joerges, C. , Meny Y., Weiler, J.H.H. (eds) (2000): *What Kind of Constitution for What Kind of Polity? Responses to Joschka Fisher*. Robert Schuman Centre for Advanced Studies, European University Institute, Florence, pp. 126-138.

Merkel, A. and F. Hollande (2013) France And Germany- Together for a Stronger Europe of Stability and Growth. Joint declaration of 21th of May, 2013, Service de Presse de la Présidence de la République.

- Merler, S. and J. Pisani-Ferry (2012 a) Sudden Stops in the Euro Area. *Bruegel Policy Contribution*, Issue No. 6, 2012
- Merler, S. and J. Pisani-Ferry (2012b) The Euro Crisis and the New Impossible Trinity. *Bruegel Policy Contribution*, Issue No. 1
- Merler, S. and J. Pisani-Ferry (2012c) Hazardous Tango: Sovereign-bank interdependence and financial stability in the Euro Area. *Financial Stability Review*, No. 16, April 2012, Banque de France
- Merler, S. and J. Pisani-Ferry (2012d) The simple macroeconomics of north and south in the EMU. *Bruegel Working Paper*, No.12/2012
- Merton, R. (1968) *Social Theory and Social Structure*. New York: The Free Press, Macmillan Publishing Co.
- Mitrany, D. (1942) "The New Deal: an interpretation of its origin and nature". *Agenda*, October 1942
- Mitrany, D. (1963) "Delusion of Regional Unity". In B. Landheer (ed.) *Limits and problems of European Integration*, The Hague.
- Mitrany, D. (1965) The prospect of integration: federal or functional. *Journal of Common Market Studies*, vol. 4, Issue 2.
- Mitrany, D. (1975) *The Functional Theory of Politics*. London: Martin Robertson & Company Ltd.
- Molino, E. and F. Zuleeg (2011) The EU budget in an era of austerity: setting the example or compensating for national cuts? *EPC workshop Document*.
- Mongelli, F. P and J. L. Vega (2006) What Effects is EMU having on the Euro Area and its Member Countries? *ECB Working Paper Series* No. 599
- Mongelli, F. P. (2008) "European Economic and Monetary Integration and the Optimal Currency Area Theory". *European Economy, Economic Papers*, No. 302
- Monnet, J. (1978). *Memoirs*. London: Collins.
- Monti, M. (ed.), 2014. *High Level Group on Own Resources: First Assessment Report*. Brussels, December 2014
- Moravcsik, A. (1998). *The Choice for Europe*. Cornell University Press.
- Moravcsik, A. (2002): In Defence of the "Democratic Deficit": Reassessing Legitimacy in the European

- Union. *Journal of Common Market Studies* 40 (4), pp. 603-624.
- Mundell, R. (1960): The Monetary Dynamics of International Adjustment Under Fixed and Flexible Exchange Rates. *Quarterly Journal of Economics* 74 (2), pp. 227-257.
- Mundlak, J. (1978). On pooling of Time Series and Cross-sectional data. *Econometrica*, Vol. 46, Issue 1, pp. 69-85
- Nicolaidis, K. (2013) European Democracy and its crisis. *Journal of Common Market Studies*, Vol .51, Issue 2, pp. 351-369
- Nicolaidis, K. and R. Howse (eds) (2001) *The Federal Vision: Legitimacy and Levels of Governance in the United States and the European Union*, Oxford University Press, p.16, p. 169
- Nicoli, F. (2013) Pathways for a Genuine Fiscal Union. *EPC Policy Brief*, June 2013.
- Nicoli, F. (2014) Populism, Polarization, Politicization, Participation. Projecting the EU beyond the Market? Chapter in: Institute of European Democrats (eds) (2014) *Rising Populism and the European Elections*. IED, Brussels, Spring 2014
- Nicoli, F. (2015) Democratic Legitimacy in the Era of Fiscal Integration. Chapter in Krieger Tim, Panke Diana and Bernhard Neumaker (eds), 2016, *Europe's Crisis: the conflict-theoretical perspective*. Baden-Baden: Nomos.
- Nicoli, F. (2016a) Euroscepticism and the Economic Crisis: evidence from a panel study of 108 elections across Europe. *Journal of Common Market Studies*, August 2016.
- Nicoli, F. (2016b) Crisis and integration: a systematic view on Europe's 70 years of unintended integration. *Working Paper*, University of Trento
- Nicoli, F. (2016c) Is the Eurocrisis a functional crisis? A quantitative approach. *Working Paper*, University of Trento
- Nicoli, F. (2016d) From Governance to Government? Towards a Genuine Economic and Monetary Union. In review at *Journal of Economic Policy*.
- Niemann, A. and P. Schmitter (2009). Neofunctionalism. In Wiener A., and T. Diez (eds) (2009) *Theories of European Integration*. Oxford: Oxford University Press
- O'Rourke, K. (2011) A tale of two trilemmas. *Discussion Paper* No. 364, Trinity College Dublin

- Obstfeld, M. (1986) Rational and self-fulfilling balance-of-payment crises. *American Economic Review*, Vol. 76, issue 1, pp.72-81
- Obstfeld, M. (1996) Models of currency crises with self-fulfilling features. *European Economic Review*, Vol. 40, pp.1037-1047
- Obstfeld, M. (1998) “A Strategy For Launching the Euro”. *European Economic Review*, Vol. 42, Issue 6, pp. 975-1007
- Obstfeld, M. (2013) Finance at the Center Stage: some lessons from the Eurocrisis. *European Economic Papers*, No. 493
- OECD (1999) *UEM: Faits, défis et politiques*. OCD Publishing, Paris
- OECD (2012), *European Union in 2012*. OECD Economic Surveys, OECD Publishing, Paris
- Olivi, B. (2000) *L'Europa difficile: storia politica dell'integrazione europea*. Il Mulino, Bologna
- Ostry, J. and A. Ghosh (2013) Obstacles to International Policy Coordination, and How to Overcome Them. *IMF Discussion Note*, December 2013
- Otjes, S. and H. Van der Veer, 2016. The Eurozone Crisis and the European Parliament's changing lines of conflict. *European Union Politics*, January 6, 2016.
- Palmeri, T. (2015) The most exclusive dining club in Brussels. *Politico*, June 18th, 2015
- Perotti, R. (2011) The Austerity Myth: Gain Without Pain? *NBER Working Papers*, No. 17571
- Peterman J.-H. (2013) Between Export Promotion and Poverty Reduction: the foreign economic policy of untying official development assistance. *London: Springer*, 2013
- Pietersen, T. and M. Bömer (2012) Economic Impact of Southern European Member States exiting the Eurozone. *Policy Brief* No. 06/2012, Bertelmann Stiftung Foundation.
- Pisani-Ferry, J. (2013) “The known unknowns and the unknown unknowns of the European Monetary Union.” *Journal of International Money and Finance*, Vol. 34, Issue C, pp. 6-14
- Pisani-Ferry, J. and G. Wolff (2012): Fiscal Implications of a Banking Union. *Bruegel Policy Brief*, Issue No. 02, September 2012
- Pisani-Ferry, J., Sapir, A., Veron, N. and G. Wolff (2012) What kind of European Banking Union? *Bruegel Policy Contribution*, Issue No. 12, June 2012

- Pisani-Ferry, J., Vihriälä, E. and G. Wolff (2013) Options for a Euro Area Fiscal Capacity. *Bruegel Policy Contribution*, Issue 01/2013
- Prodi, R. (2001) Interview with Financial Times, December 2001.
- Puhani, P. (1999) Labour Mobility - an adjustment mechanism in Euroland? *Social Science Research Network discussion paper*. No. 34
- Raunio, T. (1999): Always a Step Behind? National Legislatures in the European Union. *Government and Opposition* 34 (2).
- Raunio, T. (2012) When Europe is involved, you get problems: explaining the European policy of the (true) Finns. *SEI Working Paper* No.127, University of Sussex
- Rawls, J. (1971): *A Theory of Justice*. Cambridge: Harvard University Press.
- Reungoat, E. (2015) Mobilizing Europe in national competition: The case of the French Front National. *International Political Science Review*, Vol. 36, No. 3
- Rittberger, B. (2014) Integration without representation? The European Parliament and the reform of the Economic Governance in the EU. *Journal of Common Market Studies*, No. 52, Issue 6
- Risse, T. (2014) No Demos? Identities and Public Spheres in the Eurocrisis. *Journal of Common Market Studies*, Vol. 52, issue 6, pp. 1207-1215
- Rodrik, D. (2007) *The inescapable trilemma of the world economy*. Dani Rodrik weblog, published on June 27, 2007.
- Rodrik, D. (2011) *The Globalization Paradox: democracy and the future of world economy*. New York: Norton ed.
- Rohrschneider, R. (2002) 'The Democracy Deficit and Mass Support for an EU-Wide Government'. *American Journal of Political Science*, Vol. 46, No.2, pp.463-475
- Rosamond, B. (2005) "The Uniting of Europe and the foundation of EU studies: revisiting the Functionalism of Ernst B. Haas". *Journal of European Public Policy*, 12:2
- Roubini, N. (2011) "Greece Should Default and Abandon the Euro. *Financial Times*, September 19th, 2011
- Roubini, N. (2012) "Greece Must Exit" Commentaries, Project-Syndicate.org. May 17th, 2012
- Sachs, J. and C. Wyplosz (1986) The Economic Consequences of President Mitterand. *Economic Policy*,



April 1986, pp. 261-322

Sanchez-Cuenca, I. (2000) The political basis of support for European Integration. *European Union Politics*, No. 2, vol. 1

Sapir, A. (2011) "European Integration at a crossroad: a review essay on the 50th anniversary of Bela Balassa's Theory of Economic Integration". *Journal of Economic literature*, Vol. 49, Issue 4, pp.1200-1229

Scharpf, F. (1970) *Demokratietheorie zwischen Utopie und Anpassung*. Konstanz, Universitätsverlag

Scharpf, F. (1998) Interdependence and democratic legitimation. *MPIfG Working Paper* No.98/2, September 1998

Scharpf, F. (1999) *Governing Europe. Democratic and efficient?* Oxford, Oxford University Press.

Scharpf, F. (2000) The viability of advanced welfare states in international economy: vulnerabilities and options. *Journal of European Public Policy*, 7:2

Scharpf, F. (2002) The European Social Model: Coping with the Challenges of Diversity. *MPIfG Working Paper* No 02/8, July 2002

Scharpf, F. (2009) Legitimacy in the Multilevel European Polity. *MPIfG Working Paper*, No.01/09, p.9

Scharpf, F. (2012) Legitimacy Intermediation in the Multilevel European Polity and its collapse in the Euro Crisis. *MPIfG Working Paper* No. 2012/6

Scharpf, F. (2014) After the Crash: a perspective on multilevel European Polity. *MPIfG Working Paper*, no. 2014/21

Schelkle, W. (2012) European fiscal union: from monetary back door to parliamentary main entrance. *CESifo Forum*, 13 (1). pp. 28-34.

Schimmelfennig, F. (2014) European Integration in the Euro Crisis: the Limits of Postfunctionalism. *Journal of European Integration*, Vol.36, Issue 3, pp. 321-337

Schirm, S. (2002) *Globalisation and New Regionalism*. Polity Pr., London.

Schmidheiny, K. (2014) Panel Data: fixed and Random Effects. Short guides to econometrics, Fall 2014.

Schmidt, V. (2006) *Democracy in Europe: the EU and National Politics*. Oxford: Oxford University Press

Schmidt, V. (2015) The Eurozone's Crisis of Democratic Legitimacy: can the EU rebuild public trust and

support for European Integration? *European Economy Discussion Paper*, 2015

Schmitt, H., Popa, S. A., Hobolt, S. and E. Teperoglou. (2015): *European Parliament Election Study 2014, Voter Study*. GESIS Data Archive, Cologne

Schmitter, P. (1969) "The Neo-Functional Hypothesis about International Integration", *International Organization*, Vol. 23, pp.161-166

Schmitter, P. (1970) "A revised theory of regional integration". *International Organization*, pp. 836-868

Schmitter, P. (2002) *Neo-Neo-Functionalism*. Working Paper, European University Institute.

Schmitter, P. (2005) "Ernst B. Haas and the legacy of Neofunctionalism" *Journal of European Public Policy*, 12:2

Schmitter, P. and Z. Lefkofridi (2015a) Neo-Functionalism as a theory of Disintegration. *European University Institute Working Paper*, 2015.

Schmitter, P. and Z. Lefkofridi (2015b) Transcending or Descending? European Integration in times of crisis. *European Political Science Review*, Vol. 7 Issue 1, pp. 3-22.

Schulz, M. (2015) *Speech by Martin Schulz*, Informal Meeting of the Heads of State and Government. Brussels, February 12th, 2015

Serricchio, F. (2012) Italian Citizens and Europe: Explaining the Growth of Euroscepticism. *Bulletin of Italian Politics*, Vol.4, No.1, 2012, pp. 116-134

Serricchio, F., Tsakatika, M., and L. Quaglia (2013): Euroscepticism and the Global Financial Crisis. *Journal of Common Market Studies* 51 (1), pp. 51-54

Sinn, H.-W. (2011) The ECB's Stealth Bailout. *Vox Policy Portal*, June 1, 2011.

Sinn, H.-W. (2014) *The Euro Trap: on busting bubbles, budgets and beliefs*. Oxford: Oxford University Press.

Sinn, H.-W. and T. Wollmershäuser (2011): Target Loans, Current Account Balances and Capital Flows: The ECB's Rescue Facility. *International Tax and Public Finance*, Vol. 19, Issue 4, pp. 458-508

Sinn, H.-W. and T. Wollmershäuser (2012) Target Balances and the German Financial Account in light of the European Balance-of-payments crisis. *CESifo Working Paper* No. 4051

Snell, J. (2016) *The Trilemma of European Economic and Monetary Integration, and Its Consequences*.

*European Law Journal*, January 2016

Spiegel Online (2012). New Powers for Brussels: Germany's Schäuble Presents Master Plan for Euro.

*Spiegel Online*, October 16<sup>th</sup>, 2012

Spiegel, P. (2014) Renzi leads center-left drive to loosen fiscal rules. *Financial Times*, June 19<sup>th</sup>, 2014

Startin, N. and A. Krouwel (2013) 'Euroscepticism Re-Galvanized: The Consequences of the French and Dutch Rejections of the European Constitution'. *Journal of Common Market Studies*, Vol. 51, Issue 1, pp. 65-84

Stiglitz, J. (2015) *Interview with the Internationale Politik Gesellschaft*. Berlin, 22 September 2015.

Available at: <https://www.youtube.com/watch?v=H9EdGYyLcO0&feature=youtu.be>

Stiglitz, J. (2016a) "*The Euro: how a Common Currency threatens the future of Europe*". W.W. Norton and Company Inc.

Stiglitz, J. (2016b) "A split euro is the solution for Europe's single currency" *Financial Times*, August 17, 2016

Strauss-Kahn, D. (2012) *A tale of three trilemmas*. Speech delivered at the Cambridge Union Society the 9<sup>th</sup> of March 2012.

Streeck, W. and K. Thelen (eds) (2005) *Beyond Continuity*. Oxford: Oxford University Press.

Szczerbiak, A. and P. Taggart (2002): The Party Politics of Euroscepticism in EU Member and Candidate states. *Sussex European Institute Working Paper* No. 51.

Szczerbiak, A. and P. Taggart (2008) 'Theorizing Party-Based Euroscepticism: Problems of Definition, Measurement and Causality'. Chapter in: *Opposing Europe? The Comparative Party Politics of Euroscepticism, Volume 2: Comparative and Theoretical Perspectives*. Oxford: Oxford University Press.

Szczerbiak, A. and P. Taggart (2013) 'Coming from the Cold? Euroscepticism, Government Participation and Party Position in Europe'. *Journal of Common Market Studies*, Vol. 51, Issue 1, pp. 17-37

Tamborini, R. (2014) Transatlantic Austerity 2010-2013: a comparative assessment. *Working Paper*, Luiss European School of Political Economy.

Terzi, A. (2015) No coordination without Representation. *Bruegel*, October 8<sup>th</sup>, 2015.

Tusk, D. (2016) *Draft Decision of the Heads of State or Government, meeting within the European Council*,

*concerning a New Settlement for the United Kingdom within the European Union.*

Ümit, K. (2009) "Europe of Monnet, Schumann and Mitrany: A Historical Glance to the EU from the Functionalist Perspective". *European Journal of Economic and Political Studies*, 2009, n.2

Van Aarle, B. and K. Weyerstrass (eds) (2013) *Economic Spillovers, Structural Reforms and Policy Coordination in the Euro Area*. Heidelberg: Physica-Verlag

Van Egmond, M., Van der Brug, W., Hobolt, S., Franklin, M. and E.V. Sapir. (2013): *European Parliament Election Study 2009, Voter Study*. GESIS Data Archive, Cologne.

Van Rompuy, H., Barroso, J. M., Junker, J.-C. and M. Draghi (2012) Towards a Genuine Economic and Monetary Union. 5 December 2012.

Verney, S. (2015) 'Waking the 'Sleeping Giant' or Expressing Domestic Dissent? Mainstreaming Euroscepticism in Crisis-Stricken Greece'. *International Political Science Review*, Vol. 36, No. 3, pp. 279-295

Villeroy de Galhau, F. and J. Weidmann (2016) Europa braucht mehr Investitionen. *Süddeutsche Zeitung*, February 8, 2016

Wallace, L. (2006) "Ahead of his time: an interview with Robert Mundell". *Finance and Development*, Vol. 42, Issue 3, International Monetary Fund.

Walzer, M. (1983): *Spheres of Justice: A Defense of Pluralism and Equality*. New York: Basic Books Inc.,

Weiler, J.H.H. (1995): Does Europe Need a Constitution? Reflections on Demos, Telos and the German Maastricht Decision. *European Law Journal* 1 (3), PP. 219-258

Weiler, J.H.H. (1996): European Neo-Constitutionalism: In Search of Foundations for the European Constitutional Order. *Political Studies* XLIV, pp. 517-533.

Weiler, J.H.H. (2000) *Fischer: the dark side*. In Joerges, C., Meny, Y., and J.H.H. Weiler (eds) (2000) What kind of Constitution for what kind of polity? Responses to Joschka Fisher. The Robert Schuman Centre for Advanced Studies; The European University Institute; Harvard Law School. Firenze, November 2000, pp.236-247

Weiler, J.H.H. (2001): *Federalism without Constitutionalism: Europe's Sonderweg*. In Nicolaidis, K. and R. Howse (eds): *The Federal Vision: Legitimacy and Levels of Governance in the United States and the*

European Union. Oxford: Oxford University Press.

Werner, P. (ed.) (1970) *Report to the Council and the European Commission on the realisation by stages of a Economic and Monetary Union in the Community*. Brussels, October 1970.

Wessels, B. (2007) Discontent and European Identity: Three types of Euroscepticism. *Acta Politica*, Vol.42, pp. 287-306

Wijsman, S. (2016). Europe's Circular Illness. *Euractiv*, April 9<sup>th</sup>, 2016

Wincott, D. (2001) Looking Forward or Harking Back? The Commission and the Reform of Governance in the European Union. *Journal of Common Market Studies*, Vol. 39, No. 5, pp. 897-911

Wolf, K. D. (1999): The New Raison d'Etat as a Problem for Democracy in World Society. *European Journal of International Relations* 5 (3), pp. 333-363

Wolff, G. (2012a) Arithmetic is Absolute: Euro Area Adjustment. *Bruegel Policy Contribution*, Issue 09/2012-May 2012

Wolff, G. (2012b). A Budget For Europe's Monetary Union. *Bruegel Policy Contribution*, Issue 22/2012.

Wolff, G., Hellberg, M., Marzinotto, B., Schuseil, P., Nicoli, F., Andreicut, D. and L. Granelli (2012) An assessment of the European Semester. *Bruegel Report*, 2012.

Woolridge, J. (2010) *Econometric Analysis of Cross-Section and Panel Data*. Boston: MIT Press, Second edition

Wren-Levis, S. (2015) Was German Wage Undercutting Deliberate? *Social Europe*, December 4th, 2015

Wyplosz, C. (1997) "EMU: why and how it might happen". *Journal of Economic Perspectives*, Vol. 11 No. 4

Wyplosz, C. (2006) "European Monetary Union: the dark side of a major success. *Economic Policy*, Vol. 21, No. 46

Wyplosz, C. (2012) *The Role of the ECB in fiscal adjustment programmes*. European Parliament, Directorate-General for Internal Policies, Policy department A- Economic and Scientific Policy.

Zuleeg, F. (2015) Can the eurozone's economic governance combine political accountability, legitimacy and effectiveness? *EPC Discussion Paper*, September 2015

Zürn, M. (2000): Democratic Governance Beyond the Nation State: The EU and other International

Institutions. *European Journal of International Relations* 6 (2), pp. 183-221

*Legal Acts of the European Union*

ECOFIN (2010) Specifications on the implementation of the Stability and Growth Pact and Guidelines on the format and content of Stability and Convergence Programmes. Consolidated version endorsed by the Council on 7 September 2010.

European Commission (2013) “Towards a Deep and Genuine Economic and Monetary Union: Ex ante coordination of plans for major economic policy reforms”. *Communication of the Commission*, No. COM(2013)166.final.

European Commission (2013) “Towards a Deep and Genuine Economic and Monetary Union: The introduction of a Convergence and Competitiveness Instrument” *Communication of the Commission*, No. COM(2013)165.Final

European Commission (2015a) “Making the best use of the flexibility within the existing rules of the Stability and Growth Pact”, *Communication of the Commission*, No. COM(2015)12.final

European Commission (2015b) “On Steps towards Completing Economic And Monetary Union”, *Communication of the Commission*, No. COM(2015)600.final

European Council (2012) Conclusions of the European Council of 14 December 2012

European Council (2013a) Conclusions of the European Council of 28 June 2013

European Council, (2013b) Conclusions of the European Council of 24/25 October 2013

European Council, (2013c). Conclusions of the European Council of 19/20 December 2013.

European Council, (2014a). Conclusion of the European Council of 20/21 March 2014.

European Council, (2014b). Conclusions of the European Council of 26/27 June, 2014

European Council (2014c). Conclusions of the European Council of 18 December, 2014

European Union (2008a) Treaty On the European Union

European Union (2008b) Treaty on the Functioning of the European Union

European Union (2012a). Final Statement of the Euro Area Summit of 29 June 2012.

European Union (2012b) Treaty on Stability, Coordination and Governance

European Union (2013) Treaty Establishing the European Stability Mechanism

European Union Regulation 1017/2015

European Union Regulation 1173/2011

European Union Regulation 1174/2011

European Union Regulation 1175/2011

European Union Regulation 1176/2011

European Union Regulation 1177/2011

European Union Regulation 1303/2013

European Union Regulation 1311/2013

European Union Regulation 1966/97

European Union Regulation 1967/97

European Union Regulation 407/2010

European Union Regulation 472/2013

European Union Regulation 473/2013